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AN ANALYSIS AND EVALUATION  
OF THE SECOND FIVE YEAR PLAN  
OF  
PAKISTAN

by  
Syed Ikram Rizvi

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A Dissertation Presented to the  
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## CHAPTER I

### INTRODUCTION

#### The Problem

Pakistan is one of the underdeveloped countries of the world. Its natural resources are limited, and it is overpopulated. The average standard of living and income per capita are very low. In addition, Pakistan is a country with extreme inequality of income. The majority of the population is enjoying a mere subsistence level.

The country is overpopulated. Its annual per capita income is around \$60. Four-fifths of its people are illiterate; welfare services are limited, its villages virtually untouched by social progress...It has inherited a civil service which was trained to collect taxes and to maintain law and order but not to carry out a program of economic development. It is heavily dependent upon foreign aid.<sup>1</sup>

Under given social, political, cultural and economic conditions, the rate of acceleration at which

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<sup>1</sup>Clair Wilcox, Everett E. Hagen, Editor, Pakistan, in Planning Economic Development, p. 52.

Pakistan can be made self-sustaining, and can raise per capita income by mobilizing available net savings in the country, with a given developmental objective through the formation of a definite economic developmental plan, is very important.

Through fiscal, monetary and other policies, the total real resources for economic growth must be allocated among competing priorities so as to break through economic bottlenecks and achieve a self-cumulative rate of economic growth within the shortest possible time. Also, factors of production must be made more flexible and mobile for the achievement of an optimum rate of economic growth.

The promotion of human welfare, particularly per capita income, requires concrete and realistic planning to utilize given factors of production. Scarcity of resources requires that allocation among different investment outlets be made so as to maximize human welfare by equalizing marginal social cost with marginal social benefit in all directions.

Productivity of given factors of production must increase so that output may increase at a rate faster than the rate of increase in population. Capital formation or net savings is the pivotal point around which investment allocations are to be made so that economic growth can become self-sustaining. The optimum rate of increase in

net savings depends upon the rate of increase in productivity and the marginal propensity to save. The rate at which net savings for capital formation is to be made must be substantially high so as to bring self-sustaining economic growth.

### Purpose of the Study

The purpose of this dissertation is to give an economic evaluation of the Second Five Year Plan (1960-65) of Pakistan. Emphasis will be given to economic factors under the assumption of favorable political, social and other non-economic exogeneous factors.

The sources of accumulation of capital formation and their utilization for the attainment of economic growth will be identified, examined, and appraised. A critical review and analysis of the allocation of scarce resources will be attempted in terms of the goal of promoting mobility and flexibility of the factors of production in the long run. Monetary and fiscal measures, including the possibility of deficit financing, must also be analyzed as strategic instruments to promote an optimum rate of capital formation and a continuous rate of economic growth without becoming involved in a serious inflationary spiral.

### Importance of the Study

A continuous and high rate of economic growth may contribute to social and political stability. Extreme inequality of the distribution of income leads not only to political revolutions but may be detrimental to the achievement of increases in productivity. Especially important is the overcoming of a higher rate of increase in population if per capita income is going to be raised. However, if conspicuous luxury consumption expenditures are replaced by real investment expenditures, the rate of capital formation can be enhanced.

An appraisal of the utilization and allocation of resources within the specified period of a plan is important because effective planning can be a strategic requisite for the achievement of the desired objective of economic growth and development.

### Hypothesis

The hypothesis of this study is that capital formation and its efficient allocation, especially the development of social overhead capital, is an integral requisite for any development program and is strategic in development planning in Pakistan. An emphasis on investment in industry and basic social overhead capital must be given

in the beginning. A long-run economic growth model, with great stress on investment programming, is to be preferred to a short-run economic growth model with emphasis on consumption.

### Methodology

Two criteria will be used for an evaluation of the formation and allocation of scarce resources for the attainment of maximum social benefit. A subjective method based on "utility analysis" and an objective method based on "productivity and real output" will be applied. These two methods will be applied to the questions of: allocation of scarce real investment expenditures between the government sector and the private sector; rate of increase in productivity; the marginal propensity to save; and the optimum rate of capital formation. Accurate statistics pertaining to the micro and macro sectors of the economy (cost analysis of a firm or industry and national income) is very important for this purpose. Unfortunately, the non-monetized sector still plays a vital role in Pakistan's economy; complete information regarding different economic data is not available.

### Major Sources

The copy of the Second Five Year Plan is itself a great source of information. In this study particular



emphasis has been placed upon Design of Development, by Professor Jan Tinbergen. Other important sources are Beyond the Welfare State, by Gunnar Myrdal; Planning Economic Development, edited by Everett E. Hagen; Economic Development, by John K. Galbraith; Economic Planning in Underdeveloped Areas, by Edward S. Mason, and The Strategy of Economic Planning, by Mahbuh Al-Haq.

Besides these books, many articles, monographs, and documents, noted in the Bibliography, have been examined and utilized.

#### Organization of the Remainder of the Dissertation

The organization of the remainder of the dissertation is as follows: Chapter II describes economic planning in different types of economies. Chapter III provides an overview of the Second Five Year Plan of Pakistan. Chapter IV examines the financing of the Second Five Year Plan. Chapter V stresses the importance of and analyzes a self-cumulative process for an elastic supply of "net savings". The name of the chapter is "The Role of Monetary and Fiscal Institutions and Policies". Chapter VI emphasizes the utilization of human potentials for the optimization of economic growth. This chapter has been entitled "Human, Administrative, and Organizational Dimensions of Developmental Planning in Pakistan". Chapter VII presents the summary and conclusions of the dissertation.

## CHAPTER II

### ECONOMIC PLANNING IN DIFFERENT ECONOMIC SYSTEMS

#### Purpose and Organization

The purpose of this chapter is to compare and describe the main contours of economics, planning in a developed Democracy, in the Communist type of economy, and in non-Communist under developed economies.

The organization of the second chapter is divided into three parts and is as follows:

Under the main heading, "Planning in a Developed Democracy," subheadings are as follows: Introduction, The Role of the Governmental Sector, The Role of Private Enterprise, and Economic Growth Under Flexibility in Factors of Production.

The second part pertains to "Planning in the Communist Type of Economy," and its subheadings are as follows: The Role of the Governmental Sector; Capital Formation and Economic Growth.

The third part describes "Planning in non-Communist Underdeveloped Economies," and has these subheadings: Problems of Underdevelopment; Developmental Strategies:

A Synopsis; Requirements and Advantages of Programming; and Deficit Financing and Economic Growth.

The Concept of Planning. "The term 'planned economy' contains, of course, a plain tautology—since the word 'economy' by itself implies a disposal of available means towards reaching an end or a goal."<sup>2</sup> Planning implies the coordination of various variable factors in the future for certain purposes and ideas. Since it pertains to futuristic occurrences, revision and review of economic resources are very important to the attainment and success of desirable goals and ends. Specifically, in real life, planning or the economizing of scarce resources occurs every day. Planning leads to rationality so that realistic attainments of certain goals can be envisioned. Economic planning leads to economizing resources so that a given end can be attained through alternative means within the shortest possible time. Economic planning, whether of a long or short run type, has to take future variables (factors) into account, so that given ends through alternative means can be realized. Effective planning requires a great use of common sense, intelligence and the ability to utilize given resources for the attainment of given ends.

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<sup>2</sup>Gunnar Myrdal, Beyond the Welfare State, p. 3.

At the same time, the "economist is bound to stress ...that as things are today there are crucial differences in methods of economic planning, both between the Soviet and the non-Soviet world and between the rich and the poor non-Soviet countries. These differences cannot be overlooked in any discussion that proceeds beyond generalities of little practical consequence."<sup>3</sup>

Economic planning in developed democracies aspires to an intervention of the government sector in the free enterprise system in such a way that coordination of the total resources and a desirable rate of economic growth is achieved. Within the general framework of economic growth, an appropriate division of function between private and public sectors of the economy, and such institutions as an organized, established system of collective bargaining, full employment and price stability are fostered through the application of monetary and fiscal policies.

Economic planning in the Communistic economies is characterized by intervention by the government sector through the nationalization of the factors of production in such a way that a desirable rate of capital formation is sought for the attainment of given targets of production. Recently, however, decentralization is being

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<sup>3</sup>Gunnar Myrdal, Beyond the Welfare State, p.vi.

stressed for this particular objective as well as for more effective resource allocation. Every effort is being made to accelerate the rate of capital formation for the realistic attainment of given production targets—both consumers' and producers' goods.

Economic planning in the underdeveloped economies should be comprehensive, programmatic, aggregative or macro economic in nature. The planning idea of the attainment of definite production targets has preceded the actual implementation of allocation of scarce resources for development purposes. Most of the underdeveloped economies have been pursuing a mixed system, where aggregative real investment outlets both from the private and the governmental sectors are coordinated in an attempt to attain an optimal rate of economic growth. The governmental sector has to accumulate sufficient net savings so that capital formation, prices, incomes and profits should be settled by various sorts of collective bargaining. It has become the responsibility of the state to provide such conditions by legislation and administration, and by an umpire service of such a kind that just and equitable agreements will be reached.<sup>4</sup>

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<sup>4</sup>Ibid., p. 44.

## Planning in a Developed Democracy

Introduction. An effort is made in this chapter to find whether an optimum combination of government and private sectors can enhance the rate of growth in productivity in an economic system. In the long run, if the factors of production can be made mobile and flexible, the rate of growth in productivity will be higher than would be possible under rigidity of the factors of production.

Under economic planning, scarce resources are coordinated, allocated, directed, and utilized in such a way that a given target, such as production, is achieved consistently and efficiently. Under democratic planning, emphasis is placed upon the creation of a favorable atmosphere for private enterprise. The government's role is to formulate and implement an aggregate macroeconomic strategy so that full employment, stability, and a continuous rate of economic growth can be achieved.

The Role of the Government. "As a rule, planning in these countries has the nature of compromise solutions of pressing practical issues. It has been gradually growing, and will in all probability continue to grow, in scope and in relative importance. A major force propelling this trend towards planning has been—and continues

to be—the steady growth of the state intervention requiring coordination.”<sup>5</sup>

Planning in a developed democracy focuses upon the goal of a continuous rate of economic development and growth. The government sector tries to guide the economy in such a manner that economic stability can be sustained by utilizing factors of production at an optimum level. Through the utilization of both monetary and fiscal operations, economic fluctuations are kept within reasonable bounds. In addition, basic social overhead capital investment has been provided by the government sector.

Role of Private Enterprise. In most of the developed economies today, private enterprise plays a dominant role in the accumulation of capital. Economic development in these economies was due primarily to the initiative of individual entrepreneurship. Individual entrepreneurship led to new innovations, new technology, and new management know-how. Automation, with heavy emphasis on capital-intensive technology, has been ushered in largely under the motivation of profit maximization.

With the emergence and development of corporations and collective bargaining, policy formulation and

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<sup>5</sup>Ibid., p. 120.

decision-making functions came to revolve around vested interest and pressure groups. Bilateral monopoly and institutionalized rigidities have been established in many industries. Because of these institutional rigidities, the government sector is expected to introduce remedial rather than curative measures. Full employment of the factors of production is now often achieved only with accompanying inflation. Productivity has on occasion lagged behind the effective demand of the labor unions for higher wages. Flexibility and the mobility of the factors of production have not always been achieved.

Economic Growth Under Flexibility in Factors of Production. With resource flexibility and mobility, continuous economic growth can be realized with stability of the price level. Economic growth can generate a cumulative process of capital formation. Emphasis on a macro-economic strategy for full employment growth can muster "grass roots" effective support for economic policies, which, in turn, is a prerequisite for economic and political stability.

Most of the developed democratic countries have already achieved self-sustained economic growth. Self-cumulative growth is continuously expanded because of the competitive spirit imparted to the system.



Assimilation of the competitive spirit leads to higher levels of innovation, technology, and capital formation. The capacity of the economy for further growth is expanded continuously. In the private sector, induced voluntary net savings are mobilized for further real investment expenditures. Profit motivation dominates the outlets of private real expenditures. Production of consumer goods is stressed at the cost of production of durable goods and the installation of heavy industry. The ratio of net savings to heavy industry and producers' goods industry can be less intensively tapped, as compared to the modern democratic developed economies, in the centralized economies of communist systems.

The rate of economic growth can be enhanced progressively if an optimal combination between the private sector and the government sector can be effected. The allocation of scarce resources can be most effectively utilized for the maximization of human welfare under conditions of continuous full employment-growth. Economic development plans will be most useful if factors of production can be made mobile and flexible in the long run.

#### Planning in the Communist Type of Economy

In the communist economies, the land and capital factors of production are generally socialized, i.e.,

governmentally owned, and operated by the centralized control of the decisions of government policy makers. Highly centralized controls are imposed partly to achieve higher levels of efficiency and productivity. In the long run, however, in the process of development, they may lead to rigidities, overlapping, and inefficiency. Myrdal describes the various dimensions of centralization in Soviet planning as follows:

"Having nationalized all industry and thereafter pressed farming into forced collectivization, the state substituted for that infrastructure of voluntary organizations which had grown up in the Western countries what in effect was all-embracing, centrally-directed state control with ramifications everywhere. Even the cooperative farms used for agriculture and for many crafts and some trades, became, in effect, primarily media for central state direction, as did the network of trade unions in industry and elsewhere. This whole institutional structure, like the organs for provincial and municipal self-government, which were also built up, was tightly held together by the Communist Party, which again was organized on the monolithic principle and centrally directed."<sup>6</sup>

Role of the Government. In the Communist economy, the goals of economic planning are determined by the centralized authority of the government sector. Emphasis is given to accentuate the rate of net savings for an expeditious achievement of self-sustained economic growth. Allocations of scarce resources are made by the centralized authority of the government, especially between the production of consumers' goods and producers' goods.

Economic stability is promoted partly by trying to keep factors of production flexible and mobile.

Capital Formation and Economic Growth. Net savings are mobilized towards heavy industry and producers' goods rather than the production of consumers' durable goods. The rate of capital formation is made to accelerate, so as to reduce economic and non-economic bottlenecks. Mobility and flexibility of the factors of production are promoted for a continuous rate of economic growth. But this is accomplished at the cost of production of consumers' goods in the short run.

Particularly at higher levels of development, the rate of increase in capital formation can be raised more progressively if decentralization is practiced. Better utilization of professional ability can bring forth higher rates of innovation, technology, and know-how. Effective participation in economic planning and in its implementation, of grass-roots, will help to impart flexibility and mobility to the factors of production.

#### Planning in Non-Communist Underdeveloped Economies

"In the underdeveloped countries, the idea [of planning] precedes its realization. As economic development cannot be expected to come by itself, planning becomes a pre-condition for development, not as in the Western countries, as a later consequence of development and all the other changes

which accompanied it. The underdeveloped countries are thus compelled to undertake what in the light of the history of the Western world appears as a short cut."<sup>6</sup>

Still, the very existence of economic planning in some form often helps to impart rationality and a more realistic approach to the endeavor to break through economic and non-economic bottlenecks to economic development.

Problems of Underdevelopment. The major obstacles to development are lack of sufficient capital goods, entrepreneurship, and socio-cultural prerequisites. The capacity to absorb capital investment is limited and an optimal rate of combination of government and private sectors must be continuously evaluated so that capacity to produce both consumers' and producers' goods can be raised to a high rate as compared to the rate of increase in population growth.

Export potential must be sufficiently expanded so that capital goods and other development goods can be paid for in the long run. Emphasis must be laid upon the importation of capital and development goods to the end that heavy capital-intensive industries can be installed. Cheap, labor-intensive factories must be started, not only for the purpose of raising marginal productivity of the under- and un-employed, but also to help satisfy the

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<sup>6</sup>Ibid., p. 122.

internal market for consumers' goods. The provision of social overhead capital must be sufficient to absorb excess manpower if a solid foundation is to be built for the accrual of self-sustained economic growth in the long run.

Developmental Strategies: A Synopsis. The installation of capital-intensive industries must infuse modernization into the agricultural sector. The rate of productivity must be raised in this sector. Higher agricultural productivity is needed not only to provide consumers' goods for an increasing population, but also to produce sufficient cash crops to pay for required imports. The industrial sector must expand enough to absorb not only the sub-marginal workers in the agricultural sector, but also be able to employ gainfully the increasing level of laborers due to the population growth. This will inject both mobility and flexibility into the factors of production in the long run without which a self-sustained economic growth level cannot be attained.

The extreme inequality of income prevalent in most underdeveloped countries should be adjusted gradually; people in the higher income groups must be encouraged to enhance their net saving potential. National planning and programming can direct the investment of these potentials into the most productive channels. Direct and

indirect taxes can be manipulated in such a way that net savings can be maximized in the long run. Real investment expenditures must be encouraged and their allocation to the production of consumption-luxury goods minimized. The cherished goal of a higher rate of productivity must be stressed rather than equal distribution of income in the short run.

Technical and non-technical education must be demarcated so as to satisfy the changing needs of the economy, depending upon its phase of development. Effective "grass roots" participation and public awareness of the objectives of economic planning could be extremely contributive to economic growth and political stability.

Industry must be stimulated, partly through subsidies and direct protective measures, depending upon the stage of economic development. Myrdal expresses this point well:

"From the market point of view, being underdeveloped means precisely that, in such a country, industries do not initially have the strength to compete successively. Otherwise it would not have remained underdeveloped. It means that, without protecting the markets, there is not enough of effective demand to absorb its labor force. Labor, therefore, is employed in less productive ways, or is unemployed. Indeed, the purpose of the form of economic planning towards which all the underdeveloped countries are now steering, with the blessing of the entire world, is very much to work out a strategy for providing investment, enterprise, and demand for labor with

such a shield against competition from abroad that the national economy will be stimulated to begin development."<sup>7</sup>

However, in the long run, a competitive environment must be created for an accelerated rate of economic growth. Economic growth may, in part, be encouraged through subsidies to private enterprise. This would serve to raise productivity and keep it high. But in the long run, a competitive thrust in the private sector can be strategic for new technology, innovation, and capital formation.

Export potential depends upon the internal economy's capacity to produce. Foreign demand depends upon the price structure of exportable commodities with special reference to given substitutes. If the demand for exports is inelastic, terms of trade can be improved. Capital formation can be accentuated when labor-intensive goods are produced at home at a cheaper rate and an optimum allocation of foreign exchange earnings are devoted to importation of capital and other development goods.

The Requirements and Advantages of Programming. The capacity of the economy to produce and absorb can be continuously expanded only if the factors of production are imbued with mobility and flexibility in the long run.

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<sup>7</sup>Ibid., p. 204.

Under given alternative plans, an optimum level of economic growth can be envisioned. Allocation of scarce resources must be assigned to alternative priorities so that economic capacity to produce will be maximized over the long run.

There is a great need for the development of statistical data pertaining to micro sectors as well as macro aggregative analysis. Under programming, alternative economic priorities must be continually scrutinized relative to consistency and efficiency.

A periodic scrutiny of the consistency and efficiency of alternative priorities for economic planning is a prerequisite factor of the utmost importance in the attainment of an optimal rate of economic growth.

Optimal economic growth will proceed from the optimal combination between the government and the private sectors. Marginal social benefits and marginal social costs must be equal on all sector allocations and at the same time. The marginal social benefits accruing from all sources must be equal in order to arrive at maximum welfare.

Once self-sustaining growth is achieved, further economic growth can become cumulative.



Deficit Financing and Economic Growth. Deficit Financing can be utilized for the accumulation of a higher rate of capital formation. The absorption of idle and current savings through the sale of securities can be less inflationary if individual savings were tapped; deficits through expansion of the money supply by commercial and central banks could prove more inflationary. The long-term sale of securities could prove a valuable tool in stabilizing the rate of economic growth. The cost of long-term borrowing would be higher as compared to short-term borrowing. Long-term investment outlets must justify their rate of productivity to pay for borrowing costs. In the long run, the rate of increase in the money supply must correspond with the rate of increase in economic productivity for further capital formation. In the short run, a greater supply of money must be channeled into different savings schemes and institutions so that the rate of real investment expenditures can be kept at a high level. Inflation leads to misdirection in the allocation of scarce resources, causing impairment of productivity by stressing conspicuous consumption expenditures. In short, the allocation of scarce resources should be expanded in such a way that a socially desirable rate of economic growth will result.

### Summary and Conclusions

Economic planning in developed democracies was largely initiated, originated and implemented by private enterprise. Until relatively recently, the government sector played a secondary role.

Economic planning in the communist-type economy was originally initiated, launched and implemented through the centralized directors of the ruling party, through the nationalization of the factors of production. With the passage of time, however, decentralization has been emphasized.

Economic planning in non-communistic underdeveloped economies is being stressed under the guidance of a mixed economy; the government's role is to lay the foundation for the private sector to initiate real investment expenditure for a higher level of economic productivity. Economic and non-economic bottlenecks have to be set aside through the intervention of the governmental sector before economic initiative by private enterprise can be effective.

If factors of production can be insured with both flexibility and mobility under an optimum rate of

### CHAPTER III

#### THEORETICAL FOUNDATIONS AND OVERVIEW OF THE SECOND FIVE YEAR PLAN

##### Purpose and Organization

The purpose of this chapter is to provide an overview and theoretical foundations of the Second Five Year Plan of Pakistan.

In the first part, the mechanization of an optimum level of a piece of land (induced through monetary rewards to the small farmers for coordination) has been stressed as a strategic base for increasing productivity. Productivity can be raised when the foundation of the economy is strengthened. The mechanization of the economy, especially must begin, so that factors of production can be mobilized, leading to a self-cumulative rate of growth in capital formation. The real resources available for net savings must be sufficient to counterbalance the rate of increase in population growth for a socially desirable rate of increase in income per capita.

In the second part, the revised second five-year plan has been critically analyzed and appraised. Different

inter and intra-sectional allocation of the given scarce resources could have enhanced the rate of growth in productivity and built a strong foundation for future development.

In the third part, a critical review of the consistency of the Plan has been provided. The manner in which tied foreign loans upset the national alternative priorities has been discussed and different measures have been suggested to see if internal factors of production can be made elastic and mobile. The internal economic capacity will have to be utilized fully both in the short and long run for the attainment of a self-sustained base of economic growth.

### Theoretical Foundations of the Second Five-Year Plan

The major theoretical foundations in planning for economic development in non-Communist underdeveloped economies have to do with saving, investment, technology, population, and resource (especially labor) employment, allocation, and mobility.

To promote and maintain economic growth, net savings must become self-sustained in the long run. This process of continuous growth can only be envisioned when the factors of production are made mobile and flexible. Rationality must be substituted for the emotional and unrealistic approach to the solution of social problems.

Developmental planning is concerned with the availability of the net savings and their allocation among alternative priorities in such a way that, in the long run, a self-sustained rate of economic growth can be attained. An optimal rate of combination between the governmental sector and the private sector will have to be found (depending upon the state of economic development) so that factors of production can be utilized to the fullest capacity of the economy, both in the long and short run. The mobility and flexibility of factors of production must be sought for the attainment of a self-cumulative rate of economic growth sufficiently higher than the rate of increase in population growth. Under the theories of linear programming and maximum social benefit, marginal social cost and marginal social benefit must not only be equalized, but marginal productivity of allocation must be maximized in all directions towards the most effective allocation of scarce resources among alternative priorities.

Optimum size in the agricultural sector is extremely important for the utilization of modern technology and the latest innovations. Sufficient agricultural productivity must be achieved so that development capital imports can be paid for by needed exports. Higher population levels, generated by the present or prospective rate of population

growth, can be adequately fed only when mechanization of the agricultural sector is implemented. Monetary rewards can be awarded to stimulate cooperative and coordinative attitudes among small farmers.

At the same time, an optimum allocation of scarce resources requires the development of industry, including the installation of the steel industry. Such allocations must be adequate to satisfy the internal need for the introduction of mechanization of the agricultural sector, the installation of heavy key industries, and the production of consumers' goods.

Technical and vocational educational emphasis must be imparted to the economy so that an optimum rate of effective exploitation of human potentials can be brought about for the construction of a flexible economic system. Labor intensive programs must be coordinated with capital intensive investment outlets so that an optimal rate of economic growth, combining full employment and technological innovation will be attained in the long run.

Socially Desirable Rate of Economic Growth. Population growth is a powerful challenge in these countries for economic growth. It sets the floor for a politically acceptable rate of growth. The first thing that usually is done in the various planning commissions is to find out

the plan size that will, at the various minimums, maintain per capital income. (For a country like Pakistan, such an exercise obviously should have another dimension: determination of the investment necessary to maintain per capital income in East and in West Pakistan.) The relevance of this factor decreases if the country has already crossed this threshold of the "reproduction stage" i.e., if it has been experiencing a net per capita rate of growth in the past.<sup>1</sup>

The rate of increase in productivity and real net savings must exceed the rate of increase in population growth by a sufficient margin to bring about a socially desirable rate of economic growth. The rate of increase in productivity has a special correlation with the productive capacity of labor. The rate of increase in productivity in Pakistan, considering the overall economy, comes to 1.5 per cent per annum. ( Table I page 35) If we multiply this rate of productivity by the expected rate of increase in total workers employed, the net result would be the expected rate of growth in aggregate gross product. This aggregate gross product implies total available resources for the development of the economic objectives. The rate of required capital formation can be estimated on this basis.

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<sup>1</sup> Mahbuherl Hag, The Strategy of Economic Planning, p. 7.

Net Capital Output Ratio. As a start, we can look at Pakistan's experience with economic development during the last ten years. The net capital ratio was found to be 1.6 in the pre-plan (1951-1955) and 2.0 in the first plan (1956-1960). These certainly are low figures if compared with the past experience of the developed economies, but are not unusual in the current development experience of some of the other underdeveloped countries. For instance, India achieved a net capital output ratio of 1.8 in her first plan, and projected ratios of 2.3 and 2.6 for the second and third plans respectively.<sup>2</sup>

Capital output ratios imply the average productivity of capital. The average productivity of capital is dependent upon many variable factors such as the pattern of allocation of real investment expenditures, the choice of technology (labor-intensive or capital intensive), the availability of unutilized capacity of the economy (due to lack of inputs such as development capital goods), the existence or lack of an optimum organization with a high degree of decentralization, the ratio of depreciation charges to gross national product, the relative emphasis upon direct real investment expenditure versus social

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<sup>2</sup> Ibid., p. 58.



overhead capital investment, and the stage and level economic development. Generally, capital output ratios can be lowered (average productivity of capital raised) by such measures as: use of fertilizers instead of irrigation works; utilization of industrial capital to the optimum level; elimination of waste, inefficiency and red-tape; etc.

In Pakistan, depreciation charges are assumed to rise as a percentage of gross domestic product in the Second Plan and following plans. Given depreciation allowances, a desired growth rate in output, and the expected capital output ratio, calculation of desired level and ratio of growth in real gross investment expenditure can be made. Then, a desired marginal rate of domestic saving can be deduced, because, for optimum utilization of the productive capacity of the economy, real savings must equal real investment expenditures in the long run. Thus, this type of analysis rests upon an accurate estimate of the marginal propensity to consume and to save with the increase in the national income. Under these conditions, net capital formation can be raised to an optimum level.

The industrial sector can be induced to expand, through, e.g., tax concessions and subsidies, an optimum level of net savings can be mobilized for high level of investment expenditures. The effective use of indirect

taxation such as excise duties, sales taxes, or turnover taxes, is indicated here. These indirect taxes produce substantial revenue for government by reaching a large percentage of the consumers and taxing the lower income groups with the highest marginal propensity to consume.

Capital Output Ratios, Investment, and Population Growth. In economies like Pakistan, it is considered reasonable to assume that there would be a capital coefficient, i.e., the ratio of a unit of capital stock to output, ranging from 4 to 2, under normal circumstances. This implies simply that a rate of increase in national income from 2 to 4 per cent can be achieved through real investment expenditures of 8 per cent of the national income. A rate of increase from 3 to 6 per cent can be realized from a 12 per cent real investment of the national income.

However, the increase in per capita income must be stressed for the attainment of a self-sustained economic growth rather than merely the rate of increase in national income. If both the rate of increase in population and in national income rise by 3 per cent, the rate of increase in per capita income is zero and per capita output remains stationary. In most underdeveloped countries, the rate of increase in population amounts to 2 or 3 per cent annually. This clearly indicates that real investment expenditure may vary from 2 to 12 per cent of the national income with-

out raising per capita income. For example, with a capital co-efficient of 2, real investment expenditures at 2 per cent of national income, and an annual increase of one per cent of national income, and an annual increase of one per cent in population would merely help to maintain a given rate of income per capita under favorable conditions. And, with a capital co-efficient of 4, 12 per cent real investment expenditures would keep income per capita constant if the annual rate of increase in population were 3 per cent. Thus, investment expenditures must be from 8 to 16 per cent and the rate of population growth kept to no more than one per cent per annum to accomplish the cherished goal of an annual increase in per capita income of 3 per cent.

In other words, real investment expenditures ranging from 2 to 4 times ( $x = 3$ ) per cent where "x" stands for the rate of increase in population, is considered essential to raise per capita income by an annual rate of 3 per cent. If this is the target optimum rate of economic growth in the short run, real investment expenditure must be between 11 and 22 per cent if the rate of increase in population is 2.5 per cent. A real investment expenditure amounting to from 8 to 18 per cent becomes pivotal if the population increases by from one to 1.5 per cent. (The correlation between the rate of increase in income per capita and the rate of increase in population is described in Table I, page 35). Alternatively, a percentage reduc-

tion in the rate of population growth permits a two to fourfold reduction in the rate of net savings for capital formation to obtain a given lower rate of growth in income per capita. If the rate of increase in population is 1.5 per cent a year, then a rate of savings of 6 per cent, with a capital co-efficient of 4, is considered a stationary rate of economic growth. With a rate of increase in population of 1.5 per cent, a rate of 8 per cent in savings would raise the growth in income per capita to 0.5 per cent per annum.

### The Second Five-Year Plan

Introduction. The second Five-Year Plan (1960-65) was proposed in June, 1960. The revised version was released in November, 1961. At the outset, the plan projected a developmental expenditure in real investment of Rs. 19,000 million. The underlying thinking was to raise the GNP by 20 per cent and create 2.6 million additional jobs.<sup>3</sup> The revised version, however, envisioned a cost of Rs. 23,000, with a goal of enhancing the GNP by 24 per cent and creating 3 million additional jobs. (The projection for 1964-65 of GNP at factor cost is given on page 43, Table III).

The evaluation in this study will be confined chiefly to the revised plan. The plan will be discussed

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<sup>3</sup>Ibid., p. 174.

in the light of prices obtaining 19 1960-61. (GNP factor cost with 1964-65 projection is shown in Table I on pages 35-6). The expected rate of increase in population was 2 per cent per annum. The purpose of the plan was to raise GNP by 24 per cent, leading to an annual increase of at least  $2\frac{1}{2}$  per cent in percapita income.

The second Five-Year Plan contemplated an overall gross capital-output ratio of 3.2 per cent (see Table II,) which corresponds with the actual capital-output during the first Five-Year Plan. Comparative gross capital output ratios between the first and second Five-Year Plans is shown in Table II, page 38.

The Public Works Program and the Indus Basin Replacement Works. The public works program, at an estimated cost of Rs. 1,600 million,<sup>4</sup> had for its goal a substantial absorption of surplus labor, from rural areas particularly.

The Indus Basin Replacement Works, with a proposed investment expenditure of Rs. 3,300 million, would raise the national product. It was believed that under favorable circumstances, a target of 24 per cent rise in GNP could likely be attained. Agriculture is to account for 28 per cent,<sup>5</sup> 32 per cent of the increase is anticipated from

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<sup>4</sup> Second Five-Year Plan of Pakistan, p. 29.

<sup>5</sup> Y. Hag, op. cit., p. 137.

**TABLE I**  
**GROSS NATIONAL PRODUCT AT FACTOR COST 1954-1959**  
 (in millions of rupees)

	1954 1955	1955 1956	1956 1957	1957 1958	1958 1959	1959 1960	Projec- tion 1964-65
<b>Agri.</b>	<b>12,407</b>	<b>11,877</b>	<b>12,778</b>	<b>12,449</b>	<b>12,102</b>	<b>12,647</b>	<b>14,390</b>
Major Agri. crop	7,139	6,713	7,657	7,480	7,107	7,664	8,850
Minor Agri. crop	1,625	1,470	1,370	1,454	1,470	1,500	1,755
Live-stock	2,584	2,597	2,609	2,623	2,636	2,650	2,780
Fish-eries	1,026	1,064	1,109	859	856	900	970
Fores-try	35	33	33	33	33	33	35
Min-ing	39	43	46	51	52	53	63
Mfg.	2,151	2,488	2,698	2,805	3,010	3,150	4,460
Lrg. scale	1,112	1,428	1,608	1,702	1,885	2,000	3,200
Sml. scale	1,039	1,000	1,081	1,103	1,125	1,150	1,440
Govern-ment	1,049	1,130	1,164	1,318	1,463	1,500	1,800
Bkg.	71	75	79	100	104	110	145
Trans. & Com.	546	565	583	609	643	680	815
Ser-vices	1,672	1,705	1,727	1,749	1,784	1,800	2,160
Rent Inc.	1,108	1,109	1,124	1,139	1,159	1,180	1,387

TABLE I (Continued)

	1954 1955	1955 1956	1956 1957	1957 1958	1958 1959	1959 1960	'64 '65
Trade whlse. retail	1,871	1,851	1,997	1,987	1,961	2,000	2,400
GNP in cnst prices	20,913	20,840	22,186	22,200	22,277	23,120	27,800
In cur. prices	14,800	18,200	22,630	22,200	24,500	25,430*	30,580+
Pop. in mil.	81.3	82.5	83.6	84.7	86.1	87.5	96.2
Per cap. income in con. prices	257	253	265	262	259	264	292
Per cap. income in cur. prices	182	221	271	262	285	290	320

\* In 1959 prices, it is estimated that the general price index was 110 in 1959 as compared to 100 in 1951-52.

Source: Revised Second Five-Year Plan, p. 45.

manufacturing, and 40 per cent of the increase in the national income is planned to come from other sectors. (Table II, on page 38) explains these figures in greater detail). It was felt that due to real investment expenditures, the economy would progressively become industrialized and the share of over 16 per cent of GNP would be derived from the manufacturing sector by 1964-65.

Capital Formation. The second Five-Year Plan proposes net marginal savings of 25 per cent from additional<sup>6</sup> output created because of real investment allocations. According to past experience, the average gross savings rates have been around 5-6 per cent. (For further detailed information, please refer to Table III, page 43). In order to achieve the objective of a 25 per cent marginal increase in savings, the plan proposes additional taxation of Rs. 1750 million, and to raise the prices of a given supply of commercial products by the public corporations. These steps were taken to augment the rate of domestic capital formation for economic growth. Maximum incentives have been provided to the end that undistributed profits can be mobilized for investment by the private sector of the economy. This would help to accentuate the rate of capital formation in the economy so that the level of self-sustained economic growth can be attained within the

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<sup>6</sup>Ibid., p. 178.



TABLE II  
ESTIMATION OF NATIONAL INCOME IN SECOND PLAN<sup>1</sup>

Sector	Gross Capital Output Ratio		Percentage Contributions to Additional output	
	1st Plan (Actual)	2nd Plan (Projected)	1st Plan (Actual)	2nd Plan (Projected)
Agriculture	2.2	2.5	25%	28%
Manufacturing	2.8	3.0	36	32
Other Sectors	<u>4.4</u>	<u>3.9</u>	<u>39</u>	<u>40</u>
Total	3.5	3.2	100%	100%

<sup>1</sup>

Source: Second Five-Year Plan (revised estimates) CSO, 30, Table 14. National Income Estimates for 1955-56 to 1959-60.

shortest possible time. According to the projections of this plan, about a one per cent annual increase in per capita consumption has been proposed. The possibility that the actual rate would be higher than the given rate in the projection is one to be considered. Net savings from additional taxation (Rs. 1750 million) might not be realized because of subsidies extended to different items such as steel, etc. Other alternatives would be mobilization of public corporations in enhancing the supply prices of their

commercial products. From this analytical rationale, it becomes quite clear that the pivot of economic growth revolves around foreign exchange. The factors of production must be made flexible and mobile in order that capital imports may be paid for sufficient exports in the long run. This is the only way to achieve self-sustained rate of economic growth in the long run.

Sectional Allocation of Scarce Resources. "Five objectives were adopted by the Planning Board to guide the allocation of resources among the several sectors of the economy and among the various projects within each sector. It was the purpose of the Plan, said the Board, to increase the national income, to improve its balance of payments, to afford additional opportunities for employment, to make steady progress in the provision of social services." <sup>1</sup>

The second Five-Year Plan allocates 20 per cent of the scarce resources to agriculture and irrigation; 26 per cent to industry, fuels and minerals; and the remaining 50 per cent to economic and social overhead capital. <sup>7</sup>

Allocation of scarce resources in the transport and communications sector ignores the realizing of internal and external economies of scale through intensive utilization for an optimal rate of economic productivity. A more

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<sup>7</sup>Ibid., p. 180.

intensive utilization of the existing roadway transportation must be stressed. Effective "grass roots" participation in the economic development programs will be of help in attaining the optimal rate of economic productivity in the long run. Primary and middle-level education must be emphasized and, through the competitive system, great emphasis must be placed on technical and vocational education on the higher level. This will infuse rationality into the economic system, preparing a strong foundation upon which to build future defenses against both economic and non-economic bottlenecks. This is a major way in which a self-sustained growth rate can be achieved within the foreseeable future. Greater concentration of economic resources in particular key sectors can be achieved so that a breakthrough in various bottlenecks can be achieved. The Plan contains no major thrust against any particular bottleneck; allocations of scarce resources has not been carried out so that the optimal rate of capital formation and rate of net savings for real investment expenditures would result.

Physical Targets in Different Sectors of the Economy. Many physical production targets for the second Five-Year Plan of the economy have been achieved or nearly achieved. Food grain targets, for example, are within visible distance, although favorable weather conditions

could have been a factor in helping to realize these targets. The rate of increase in industrial production has been about 12 per cent per annum and it may very well go higher, according to Plan targets, viz., 60 per cent within the span of this particular plan.<sup>8</sup> Installed power generating capacity increased by 30 per cent and demonstrative capacity of actual operation went up by re per cent during the first two years of the Plan. Progress in the transport sector is satisfying.

The target for commercial crops, particularly cotton, has woefully lagged behind. This adversely affected the capacity of exportable surplus in the economy. The actual producible supply in key industries such as cotton textiles, jute goods, cement, sugar, coal and natural gas has not been up to expectations. The actual rehabilitation target for displaced persons might not be achieved, and adequate and sufficient emphasis on primary education has been lacking.

Role of the Government Sector and the Private Sector. The optimal rate of combination of the government and the private sectors is extremely important in the attainment of a desirable rate of marginal net savings and a cumulative rate of productivity. This is another strategic means through which a higher rate of self-sustained

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Ibid., p. 190.

economic growth can be achieved within the shortest possible period of time.

Under the theory of programming and maximum social benefits, not only must management, expansion, and direction of private investment expenditure be emphasized and implemented, but also more and better statistical data must be compiled and made known. Investment priority choices of the private sector must be influenced by monetary inducements, subsidies, tax concessions, and various types of subventions of government.

Consistency and Efficiency. In the Second Five-Year Plan, allocation of scarce resources according to the criteria of consistency and efficiency for a continuous rate of capital formation, apparently has been ignored. Consistency and coherence between the macro sectors, such as firms, products, costs, and prices, and the macro aggregative sector, such as national income and the level of employment, have not been satisfactorily achieved. Consistency between the physical and financial planning targets have been discarded. Within the context of efficiency consideration, the Plan could not justify the allocation of scarce resources to the agricultural sector. Under Pl. 480 aid free importation of surplus food grains to the extent of 8,722 millions could have helped the supply of

**TABLE III**  
**INCOME, INVESTMENT, SAVINGS AND**  
**CONSUMPTION IN THE SECOND PLAN**  
**(1960-61, in millions of rupees)**

	1959-60	1960-61	1961-62	1962-63	1964-65
(1) Gross National External Resources	30,000	31,780	33,440	35,100	37,270
(2) Rate of Growth	---	5.9%	5.2%	5.0%	6.2%
(3) Gross Invest- ment	3,050	3,120	3,840	6,650	5,910
(4) (3) as of (1)	10.2	10.0	11.4	13.2	15.9
(5) Gross Domestic Saving	1,820	2,030	2,370	2,300	3,270
(6) (5) as a % of (1)	6.0	6.4	7.1	6.5	8.8
(7) External resources	1,300	1,120	1,430	2,300	2,640
(8) (7) as a % of (1)	4.3	3.5	4.3	6.5	6.5
(9) Total Con- sumption	28,250	29,690	31,070	32,750	34,000
(10) (9) as a % of (1)	94.0	93.5	93.0	93.0	91.2

NOTE: Columns (5) and (7) do not add up to column (3) because of changes in foreign exchange reserves.

Source: Government of Pakistan, Planning Commission, Mid-Plan Period (March, 1963).

**TABLE IV**  
**SECTORIAL ALLOCATION IN THE**  
**SECOND FIVE-YEAR PLAN**  
**(in 1960-1961 prices)**

Field of Development	Allocation (million rupees)		Percentage Share	
	Private	Public	Total	
Agricultural	900	2,520	3,420	15%
Irrigation	nil	2,050	2,050	9
Sub-total	900	4,570	4,570	24
Industry	3,600	1,460	5,120	22%
Fuels & minerals	550	450	1,000	4
Sub-total	4,110	1,190	6,120	26
Transport & Communication	1,330	2,720	4,050	18%
Power	250	2,090	2,340	10
Housing & Settlements	1,520	1,890	3,410	15
Education & Training	100	950	1,050	4
Health	50	370	420	2
Manpower & Social Welfare	20	120	140	1
Sub-total	3,270	8,140	11,410	50%
Grand Total	8,380	14,620	23,000	100%

Source: The Second Five-Year Plan (revised estimates)  
Table 1.

cash crops for export, bringing a higher level of foreign exchange which could have been used for the importation of development goods.<sup>9</sup> Pl. 480 imported surplus food grain, while supplies were lying unsold in godowns could have been substituted for the production of food grain supply. This could have helped to enhance the producible capacity of the economy of cash crops which forms a great source of foreign exchange earnings.

### A Critical Review of the Consistency of the Plan

Lack of Economic Statistics. Accurate estimates pertaining to the different components of private investment outlets and domestic savings are not available. Total taxable capacity cannot be appraised as long as accurate data pertaining to the distribution of per capita income are not available. To formulate programs for maximum social benefit, accurate approximations relating to the private sector's real investment expenditure, domestic rate of capital formation, the investment component of foreign exchange availability, and the distribution of income, are all extremely important.

Rate of Increase in Productivity. Implementation of the various economic programs must be scrutinized to assure that marginal productivity becomes equal in the



**TABLE V**  
**COMPARISON OF ALLOCATIONS**  
**IN THE FIRST AND SECOND**  
**PLAN**  
**(Percentages)**

Field of Development	First Plan (proposed)	Second Plan (proposed)
Agriculture	11%	15%
Irrigation	12	9
Sub-total	23%	24%
Industry, Fuels and minerals	28%	26%
Power	8	10
Sub-total	36%	36%
Transport & Communications	17%	18%
Housing & Settlements	14	15
Education	4	4
Health	2	2
Social Welfare & Manpower Training	1	1
Miscellaneous	3	1
Grand Total	100%	100%

Source: Annual Budgets (Central and Provincial Governments)

TABLE VI

PHYSICAL PRODUCTION TARGETS AND ACHIEVEMENTS OF THE  
SECOND FIVE-YEAR PLAN  
(For the first two years)

Sector and Sub- Sector	Production			Percentage Change Over Base Period		
	Base Period	1960-61	1961-62	Plan Target	1960-61	1961-62
Agriculture						
(a) Food grains 000tons	13,189	15,412	15,867	21	17	20
rice 000 "	8,341	10,533	10,575	22	26	27
wheat 000 "	3,703	3,786	4,064	17	2	10
(b) Cash crops						
jute 000bales	6,000	5,626	6,969	22	6	16
cotton 000 "	1,666	1,711	1,840	38	3	10
sugar cane 000 "	15,430	15,412	18,548	35	negative	20
tea mil. lbs.	54.3	42.0	58.8	18	-23	8
Industry, fuels and Minerals						
Cot. yard mil. lbs.	380	408	423	37	7	11
jute goods 000tons	250	249	271	52	negative	8
cement 000 "	1,050	1,142	1,287	186	9	23
sugar 000 "	150	110	181	100	-26	21
coal 000 "	723	784	900	107	8	24
natural gas, billion cu.ft.	25.8	32.2	44.0	287	24	70

Source: (a) Generally, 1959-60 used as base year, except in certain cases in the Agri. Sector, where the average of a few years was taken.

(b) Estimated level of production 1964-65

Mid-Plan Review, p. 95.

various sectors of the economy. The pace of economic development can be maximized only if marginal productivity, is brought to an optimal rate in all of the sectors. It appears that productivity for implementation in the transport and communications and the water and power sectors is higher than that found in social services, education, and the agricultural sectors.

The relationship of costs and benefits to implementation of different economic programs must be adequately analyzed when prices tend to rise in a developing country. Cost-benefit ratios are often miscalculated because of inadequate engineering, wrong approximations as to price trends, and uneconomic implementation. Most of the projects would have been discarded had their costs and benefits been fully known prior to their implementation. However, precise and correct approximations concerning price trends and certain uneconomic implementations, could have been made through the interpretation of the information contained in the following table. It shows the discrepancy between the original and the final cost involved in the implementation of certain projects.

In a developing economy, where real expenditures are being allocated between steel and other heavy industries, and light goods and consumers' goods industries, the supply of goods producible in the short run lags behind the

TABLE VII  
ORIGINAL AND FINAL COSTS OF 4 PROJECTS<sup>10</sup>  
(In millions of rupees)

PROJECT	Original Cost (est.)	Final Cost	Percentage Increase
Ganges-Kohadak (Kashtra Unit)	20	188	890%
Kurrans-Garhi (Multipurpose)	10	76	660
Teestra Barrage Project	99	405	309
Kasnaphuli Multi- purpose Project	254	489	93

increasing level of generated income. This causes a rise in supply prices to satisfy the higher effective demand. The original Plan size of Rs. 19,000 has been revised upward to Rs. 23,000 million after only one year of operation.<sup>11</sup> The influence of domestic decontrol measures and insistence by foreign countries on "tied credits" have affected the general price level. Since the latest revision (1960-1965) the price level has risen by 7 per cent. It appears reasonable that Rs. 25,000 million will be required to implement the Plan size of 23,000 million.

<sup>10</sup>Hag. op. cit., p. 193.

<sup>11</sup>Ibid., p. 194.

The Nature of Foreign Assistance. Much of the current Pakistan development program is financed in real terms by foreign assistance. This foreign assistance is project-type, and should be made more flexible. This is another strategic way in which the rate of self-sustained economic growth can be assured within the shortest possible period of time. It is in the best interests of a higher rate of net savings and the optimal rate of increase in productivity in the long run.

Project-type assistance becomes the pivot around which national alternative priorities revolve for their effective implementation. While it is comparatively easy to sell big, well-engineered hydro-electric and transport projects, smaller projects in the fields of agriculture, education and social sciences often encounter some difficulty. But a more effective concentration of the allocation of scarce resources to these latter sectors might prove more productive in increasing the cumulative rate of capital formation over the long run.

The importance of the Consumption Function. Much attention has been concentrated on the feasibility of production targets. Adequate and proper attention also must be given the rate of marginal consumption expenditures with the increase in the income level, and definite

steps taken to ensure compatibility between effective demand and supply of goods. It has been assumed that the overall annual increase in per capita consumption would be about one percent. However, there are no reliable statistical data pertaining to the distribution of marginal income; consequently, the effects of marginal consumption expenditures are not known. A precise demand for certain commodities, due to effects of marginal consumption expenditures (because of increase in the level of income brought about by real investment expenditures), must be analyzed. Approximately 50 per cent of the gross investment expenditures is projected as provided by foreign resources.<sup>12</sup> The net rate of savings and capital formation, along with the rate of productivity, must rise higher than the rate of increase in population if an effective accrual of self-sustained economic growth is to be realized.

The Importance of Effective Programming. According to the theory of programming, there should always be alternative priority allocations so that the rate of capital formation can be brought to the optimum in the long run. In the alternative priority allocations, heavily concentrated optimum allocations should be assigned to the exploitation of fuels and minerals. An organization with

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<sup>12</sup>Ibid., p. 195.

decentralized authority can save up to 5 per cent of these allocations from all sectors. About one-half the allocations to the agricultural sector could have been saved through the effective use of surplus food grains under PL 480 aid in the amount of \$722 million.<sup>13</sup> An adequate supply of cash crops for foreign exchange earnings could easily have been produced. Concerning the transport and communications sector, intensive utilization could have brought forth economics of scale, e.g., by concentrating sufficient thrust to road utilization instead of spreading these scarce resources throughout the transportation and communication sectors. A higher percentage of these resources could have been diverted to fuels and minerals; a larger percentage could have been deducted from manpower and social welfare sectors. To achieve self-sustained growth, an enhanced productivity must take precedence of the distribution of income in the short run.

### Summary and Conclusions

An optimum level of a piece of land and the very mechanization of the agricultural sector is an important pre-requisite for a long run socially desirable rate of economic growth.

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<sup>13</sup>Ibid., p. 184.

The availability of net real savings are dependent upon the rate of growth in productivity. A cumulative rate of real savings are very essential for the attainment of long-run economic growth.

The average productivity of capital (output capital ratio) will be low in the beginning, but with the advancement of economic growth, can be raised to a substantial degree.

Real savings in the long run must be sufficient to infuse both flexibility and mobility into the factors of production for a self-sustained rate of economic growth. The rate of real savings and real investment expenditure must be substantially higher so as to induce a higher rate of growth in productivity as compared with the rate of increase towards growth in population.

The Revised Version of the Second Five-Year Plan was extended to Rs. 23,000 millions instead of Rs. 19,000 millions according to the first draft of the second Five-Year Plan. This was done to enhance the GNP by 24 per cent instead of 20 per cent. The average gross capital-output ratio was 3.2 as compared with 3.5 available during the first five year plan.

Besides the second Five-Year Plan, the Public Works Programme at an estimated cost of Rs. 1,600 millions, and the Indus Basin Replacement works with a proposed



investment expenditure of Rs. 3,300 millions, were also launched.

Most of the physical targets have been attained, though in the future, the contribution from the industrial sector towards the GNP (gross national product) is expected to be higher compared to the agricultural sector.

The average gross savings rate has been about 5-6 per cent. Net marginal saving of 25 per cent was envisioned. Through more taxation and other measures, the net marginal savings was expected to be raised to attain a self-cumulative growth rate.

The allocation of planned investment resources was 20 per cent for the agricultural and irrigation sector; 26 per cent to the industry and fuels and minerals; with the remaining 50 per cent to economic and social overhead capital. Different intra-sectoral and inter-sectoral could have attained a higher rate of productivity from the given allocations.

Lack of sufficient data pertaining to the micro and macro sectors of the economy, especially for the coordination of both the private and the governmental sectors, are not available so that allocations on alternative priorities for maximum productivity could have been analyzed.

Attempts should be made to have united types of economic assistance from foreign resources so that scarce

resources can be allocated to alternate priorities for the attainment of self-sustained level of economic growth, within the shortest possible time.

The importance of the consumption function should not be overlooked. The capacity of the economy to produce sufficient consumers' goods is limited, particularly in the short run. With the intensive programs of real investment expenditures, real savings may be encouraged sufficiently so as to maintain a continuous rate of economic growth without being involved in an inflationary spiral.

## CHAPTER IV

### FINANCING OF PAKISTAN'S SECOND FIVE-YEAR PLAN

#### Purpose and Organization

This chapter explores the financing of Pakistan's Second Five-Year Plan. Although real resources must be the pivotal point around which the selection of alternative priorities must be considered, financing of the plan is strategic. Net savings out of domestic resources must be expanded to attain flexibility in the factors of production, as explained earlier. The ratio of loans to total foreign assistance will significantly affect attainment of social maximum benefit in the long run. Net foreign assistance (by deducting tied loans), with the implicit intention of the importation of capital goods and other developmental goods, contributes to explaining the rate at which capital formation can be made flexible in the economy itself. Future export potentials are highly dependent upon the sources of importation of different types of goods. Deficit financing can also be a contributing factor toward the accentuation of the rate at which capital formation can become cumulative. The rate of growth in productivity can be continued only if confidence

through consistency within a given supply of net savings for the implementation of different projects can be materialized.

The organization of this chapter is as follows:

"The first part provided an introductory statement pertaining to the purpose and organization of the chapter. The second part endeavors to elaborate the financial requirements of Pakistan's Second Five-Year Plan, giving an overall view. In the third part, some explanations have been made regarding the sources of funds during Pakistan's Second Five-Year Plan, with discussion of each individual source. The fourth part of this chapter is related to the role of foreign aid, trade, and exchange in financing the Second Five-Year Plan."

TABLE I

Original Estimates (in crore rupees)				Revised Estimates (in crore rupees)		
<u>Requirements</u>	<u>Local Cur- rency</u>	<u>Foreign Cur- rency</u>	<u>Total</u>	<u>Local Cur- rency</u>	<u>Foreign Cur- rency</u>	<u>Total</u>
Second Plan	1,250	650	1,900	1,455	845	2,300
Maintenance*						
Needs	-150	+150	---	-250	+250	---
Net 2nd Plan	1,100	800	1,900	1,205	1,095	2,300
Indus Basin						
Replacement						
Works	108	135	243	144	186	330
Works Program	---	---	---	122	38	160
Total Require- Ment	1,208	935	2,143	1,471	1,319	2,700

\*Maintenance support will generate rupee resources which have already been taken into account in calculating the availability of rupee resources for the Plan.

Source: Table V, p. 22      Revised Second Plan.

Ten million = one crore. United States \$1.00 = 4.75 Pakistan rupees.

### Financial Requirements of Pakistan's Second Five-Year Plan

The total requirements for the original Second Five-Year Plan amounted to 2, 143 (crore rupees),<sup>14</sup> out of which 1,208 (crore rupees) were available in Pakistan's currency and the rest 935 (crore rupees) were in dollar currency. The revised Plan was projected to the extent of 2,740 (crore), out of which 1,471 (crore of rupees) were in local currency and 1,319 were in dollar currency.

The maintenance needs imply the depreciation allowances through which full industrial capacity can be kept continually fully utilized. If depreciation allowances are not accounted for, a substantial part of the industrial capacity could not have been tapped for economic growth. The requirements for depreciation charges from the industrialized economies would tend progressively to go down with the expansion in export potential and the development of import substitutes within its own economy. This is possible only if the internal economy, through optimum mechanization, is sufficiently capable of producing an elastic supply of depreciation consumption goods so that substitution of those goods which are to be imported for the maintenance of full existing and new industrial capacity, can be visualized.

The difference between the Second Plan and the

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<sup>14</sup>

Revised Second Five-Year Plan, p. 22.

"Net" Second Plan requirements would be the inclusion of depreciation charges for goods and related materials, in the latter case so that the existing or new capacity of the economy can be kept fully employed. The depreciation allowances (charges for goods and related materials) are highly dependent upon the elastic supply of importation of development goods and other auxiliary capital goods. Their needs can be met only through the availability of foreign exchange components dependent upon the stage of economic development, or on the elastic supply by the native factors of production.

The Requirements of the Indus Basin Project. Regarding the original estimates, total requirements were to the extent of Rs. 243 (crore), out of which total currency amounted to Rs. 108 (crore) and Rs. 135 (crore) were in foreign currency. On the other hand, in the revised estimates, local currency stood at Rs. 144 (crore) but the amount of foreign exchange amounted to Rs. 186 (crore). Total expenditure of Rs. 330 crore (\$693 million) was partly financed from counterpart funds to the extent of Rs. 106 crore (\$223 million).<sup>15</sup> The rest (Rs. 224 crore-\$470 million) was secured in foreign exchange under the auspices of the World Bank through grants and loans.

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<sup>15</sup>Ibid., p. 27.

A supply of surplus foreign exchange of Rs. 38 crore (\$80 million) ensued because the foreign exchange component required for this project stood at only Rs. 186 crore (\$390 million). It was contemplated that this foreign exchange surplus (Rs. 38 crore or \$80 million) would be utilized to purchase Pakistani rupees from the State Bank of Pakistan. Utilization of this foreign exchange surplus was directed toward provision of the importation of commodities so that inflationary effects generated due to the investment outlays on the Indus Basin Works could be neutralized. Moreover, the expanded PL 480 program helped to increase the capacity of the economy to resist inflation, through increased supplies of essential commodities. This was responsible for insuring a continuous rate of productivity resulting from the PL 480 financing of this program and higher ability to dispense with deficit financing consequent upon the increased supply of rupee resources.

Requirements of the Works Program. According to the revised estimates, Rs. 160 (crore) were needed for the implementation of this Works Program.<sup>16</sup> Out of the Rs. 160 (crore), Rs. 122 (crore) were required in local currency and, on the other hand, Rs. 38 (crore) were to be secured in foreign currency so that the program could be materialized. In short, Rs. 160 crore (\$336 million)

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<sup>16</sup>Ibid., p. 29.

were made available for the fulfillment of the Works Program. This amount was to be utilized for the provision and distribution of essential commodities, small equipment and such other imported raw materials required for the adequate implementation of the Works Programme.

The main objective of this program was to mobilize the underutilized manpower of Pakistan by putting the men to work on nation-building projects. The main sectors to benefit from the program were: coastal embankments low-lift pumps, small irrigation schemes, water supply, drainage, low-cost housing, school construction, feeder roads, etc.

The Reason for the Separation of Listings. There are two reasons for this classification: (1) mostly they are financed through the creation of the PL 480 program conducted between the governments of the United States and Pakistan and (2) the required foreign exchange to make up any deficiency in the importation of adequate development and non-development goods can be accessible through the auspices of the World Bank. Precisely, the contributions through internal productivity of the economy are negligible for the implementation of the development plans.

Government and the Private Sector. The governmental



sector is supposed to cement the foundation of the economy so that an optimal combination between government and private sectors would be able to impart a desirable rate of economic productivity interruptedly. Agricultural productivity should be raised sufficiently to counterbalance the higher rate of population growth. For the attainment of this objective, the optimal accrual of the metallic base of the economy must be materialized during the initial steps of the economic development programs.

In the second Five-Year Plan, sufficient emphasis toward a long-run model has not been made. Neither have allocation of scarce resources or alternative sectoral priorities been handled in a manner so that intensive utilization of the PL 480 program would assume responsibility for increased export potential through higher production of cash crops. Table Ia the comparative investment outlays demarcated between the government and the private sectors. In the original Second Five-Year Plan, governmental development outlays were 61 per cent as compared with 39 per cent undertaken by the private sector, while in the revised plan, the governmental sector invested to the extent of 64 per cent and the private sector was responsible for 36 per cent of aggregate outlays.

TABLE IA \*

## RESOURCES FOR THE GOVERNMENT FINANCES SECTOR

1964-1965 (Crore Rupees)

	<u>Original Plan</u>	<u>Revised Plan</u>
<b>Sources:</b>		
Surplus on Revenue Account	80	122
Net capital receipts	150	140
Local bodies	20	20
Sales Proceeds of Commodity Aid	300	420
PL480 Counterpart Funds	---	60
Project aid & Loans	400	525
Additional taxation	100	175
Deficit financing	100	---
<b>Total</b>	<b>1,150</b>	<b>1,462</b>
<b>Uses:</b>		
Public Sector's Own Development program	975	1,240
Loans to Semi-public Sector	175	222
<b>Total</b>	<b>1,150</b>	<b>1,462</b>

\* Source: The Second Five-Year Plan, p. 23.

TABLE II \*

MAJOR SOURCES OF FUNDS FOR PAKISTAN'S  
SECOND FIVE-YEAR PLAN

	<u>Original</u>		<u>Revised</u>	
	<u>Crore(Rs.)</u>	<u>Per Cent</u>	<u>Crore(Rs.)</u>	<u>Per Cent</u>
Saving	750	39%	758	33%
Taxation	250	13%	387	17%
Foreign Aid	800	43%	1,115	50%
Deficit Financing	<u>100</u>	<u>5%</u>	<u>---</u>	<u>---</u>
<b>TOTAL</b>	<b>1,900</b>	<b>100%</b>	<b>2,300</b>	<b>100%</b>

\* Source: Ibid., p. 22.

### Sources of Funds for Pakistan's Second Five-Year Plan

The strategy for development in Pakistan has been to channel resources to those groups in the community whose average and marginal saving ratios are thought to be relatively high. In practice, this has meant that income was redistributed away from the massive agricultural population, in favor of the small class of wealthy, urban industrial entrepreneurs. The surplus thus accumulated and available for investment was to be guided into high priority projects through the use of indirect (monetary and fiscal) controls. After the unhappy experience of the early 1950's there has been a general tendency to avoid direct controls, state ownership of industries, and government intervention.<sup>17</sup>

According to the comparative allocations of this Plan, Table II, above, was prepared. Total savings comprise Rs. 750 (crore) and 39 per cent of the given original investment outlays, whereas according to the revised version of the Plan, savings amounted to Rs. 758 (crore), or 33 per cent of the total outlays.

Taxation was responsible for the accumulation of Rs. 250 (crore) or 13 per cent of the original Plan. Rupees 387 (crore) or 17 per cent were collected out of

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<sup>17</sup>Keith B. Griffin, "Financing the Development Plan in Pakistan," Pakistan Development Review, (Winter, 1965) p. 603.

the revised version. Foreign aid amounted to Rs. 800 (crore) or 42 per cent of the original Plan and Rs. 1155 (crore) or 50 per cent were available in foreign aid according to the revised version. Deficit financing was to be resorted to in the amount of Rs. 100 (crore) or 6 per cent of the original plan. There was no deficit financing in the revised plan. The total amount of Rs. 1900 (crore) was projected according to the original plan but this amount was raised to Rs. 2300 (crore) during the revised version.

Advantages and Disadvantages of the Four Major Sources of Funds. Savings: Real savings were extremely important prerequisites for imparting flexibility and mobility in the factors of production. Real savings transformed into real investment expenditures are responsible for a cumulative rate of capital formation; they become a pivotal point around which a socially desirable rate of economic growth can be materialized, especially if the rate of increase in population growth can be slowed down. At the same time, too much real savings, in the quest for an increase in the rate of productivity, could very well be at the expense of reducing consumption to a mere subsistence level. An optimum combination of real savings and real consumption will have to be demarcated

Taxation: An elastic rate of taxation could be very important in the maintenance of economic stability as well as for a continuous rate of productivity in the entire economic system. Taxation can be raised to achieve a desirable rate of real investment expenditures and their allocation to various alternative priorities. Too much taxation could lead to misdirection of real resources, however, thereby causing a lower rate of economic productivity through adversely affecting the incentives to work, to produce, to save and to take risks.

Foreign aid.--In the initial stages of economic development, the economies of underdeveloped countries can be rendered highly productive by the importation of both capital and development goods. Social overhead investments could help to build a sound foundation upon which a self-sustained level of economic growth could be expected in the long run. Tied foreign aid might serve to upset the allocation for alternative priorities in the interests of achieving the maximum social benefit, however. Also, the economy might find it difficult to absorb an excess of foreign aid, thereby leading to unproductive investments.

Deficit finance. Taxable capacity and expenditures through deficit finance must be equalized in the long run. Long-run maturities with adequate timing and spacing could

be helpful in controlling inflation and in maintaining a stable rate of economic growth. However, excessive deficit finance reaching beyond the full capacity of the economy would lead to inflation and misdirection of real resources. This could prove extremely detrimental to long run economic growth.

TABLE III \*  
DETAILED STATEMENT OF SOURCES OF FUNDS

Sources of Funds	Original Five-Year Plan		Second Five-Year Plan	
	Crore(Rs.)	Per Cent	Crore(Rs.)	Per Cent
1. Savings	750	39%	758	33%
a. Net Capital receipts	150	8	140	6
b. Private savings, including public utilities' own resources	600	31	618	27
2. Taxation	250	13%	387	17%
a. Revenue surplus	80	4	122	5
b. Additional taxation	100	5	175	8
c. Local bodies	20	1	20	1
d. Customs on Commodity Aid	50	3	70	3
3. Foreign Aid	800	43%	1,155	50%
a. Project aid & Loans	490	26	685	30
b. Foreign private investments	60	3	60	2½
c. Commodity aid	250	13	350	15
d. P.L.480 Counterpart funds	---	--	60	2½
4. Deficit financing	100	5%	---	--
TOTAL	19,000	100%	2,300	100%

\* Source: Ibid., p. 40

**Sources of Funds During Pakistan's Second Five-Year Plan:**  
**Further Discussion**

**Introduction.** Sources of funds must be made elastic with the transformation of the underdeveloped economies from agricultural primitive stage to industrial economy. Underdeveloped countries should be able to impart flexibility in the factors of production so that their foreign exchange earnings could be made more elastic. Their very economic survival may be at stake if agricultural productivity is not enhanced to an optimum level through mechanization. This however, could be materialized only if political rigidities and social and economic bottlenecks can be set aside through emphasis on the availability of an optimum level of savings. The capacity of the economy can only be fully utilized if an adequate supply of capital goods and development goods can be imparted by catering to the needs of economic productivity.

**Detailed Discussion.** There were four sources of funds which facilitated the implementation of Pakistan's Second Five-Year Plan. These four sources were (1) savings, (2) taxation, (3) foreign aid, and (4) deficit finance.

**1. Savings.**

**a. Net capital receipts.** Net capital receipts amounted to Rs. 140 crore (\$294 million) during

the revised plan period. Chief sources of these receipts were small savings, public borrowings from non-bank sources, sale of PIDC (Pakistan Industrial Development Corp.) assets, depreciation and other reserve funds. For the original plan these receipts stood at 150 crore. Small savings rose from Rs. 24 million in 1950-51 to Rs. 68 million in 1954-55. The main reason for this substantial increase was due to special impetus through higher yields on small savings certificates. Public borrowing from non-bank sources such as individuals, insurance companies, trust and joint stock companies, stood at 95 million in 1959. Approximately Rs. 200 million of Pakistan Industrial Development assets had been sold to the private sector.

b. Private savings (including public corporations' own resources).

These savings amounted to Rs. 618 crore (\$) for the revised plan, whereas for the original plan, it was only 600 crore. —

Total private savings for the whole original plan were 31 per cent, whereas for the revised



plan there was a decrease to 27 per cent. The sum of Rs. 618 crore (\$1,298 million) was contributed by the net savings of public corporations and the private sector. Borrowing of the private sector through the banking system had been around Rs. 200 crore (\$420 million) and net capital formation mobilized through the stock exchange stood at about Rs. 50 crore (\$105 million).

## 2. Taxation.

a. Revenue Surplus. The revenue surplus for the original plan was 80 crore (rupees). There were projections for an adequate revenue surplus to cope with the new development expenditure of the public sector. The administrative expenditure of the government rose by over 4 per cent annually, but the burden of recurring liability with sequence to development schemes went up to the extent of 14 per cent annually. Defense expenditure had been accounting for nearly 40 per cent of aggregate expenditure of the government (about 3.5 per cent of gross national product). The recurring cost of development schemes in certain sectors, such as education and health, had been around Rs. 150

million in 1959-60, and the total liability was Rs. 750 million during the second plan period.

b. Additional taxation. The imposition of additional taxation was to yield 100 crore rupees in the original plan, but in the revised plan it was raised to 175 (crore rupees). Additional taxation during 1960-61 brought revenue to the extent of Rs. 12 crore (\$25 million). Total revenue through the revised plan stood at Rs. 75 crore (\$158 million) and it was projected to raise another Rs. 100 crore (\$210 million) during the last four years.

c. Local Bodies. The Institution of Basic Democracies had been empowered to levy taxes; total accrual from this source was 20 (crore rupees) both in the original and revised plans.

d. Customs on commodity aid. This helped to raise 50 (crore rupees) in the original plan, where as in the revised plan it amounted to 70 (crore rupees). Accrual from taxation in the original plan was 12 per cent, but in the revised plan it was raised to 14 per cent.

### 3. Foreign aid.

a. Project aid and Loans. The total amount of project aid and loans in the original plan was

Rs. 490 (crore) or 43 per cent. This sum was raised to Rs. 685 (crore) in the second revised plan or 50 per cent. The total amount of this aid secured by the government sector stood at Rs. 875 crore (\$1,838 million). This exceeded its actual requirement (Rs. 453 crore or \$952 million) by Rs. 422 crore (\$886 million). This excess of foreign exchange was sold to the semi-private sectors; these sectors utilized Rs. 250 crore (\$525 million) toward their maintenance support and the balance of Rs. 172 crore (\$361 million) for their economic development projects. In addition to this, a sum of Rs. 220 crore (\$462 million) was directly available to them in the form of foreign aid. Public corporations were responsible for the attraction of private foreign investment, mainly in oil and gas explorations, to the extent of Rs. 60 crore (\$126 million). Moreover, Rs. 75 crore (\$158 million) was diverted to Pakistan Credit and Investment Corporation (PIDC) and Rs. 60 crore (\$126 million) was loaned to Pakistan Industrial Development Bank (PIDB) and direct loans were advanced to other public corporations to the extent of Rs. 25 crore

(\$52 million).

b. Foreign private investment. The total foreign private investment available during the original plan was 60 crore rupees; in the revised plan the amount remained the same.

c. Commodity aid. Commodity aid from the United States, Canada, and other countries was projected at Rs. 250 crore (\$525 million) for the original plan. In the revised plan this projection was raised to Rs. 350 crore (\$735 million) composed of Rs. 250 crore (\$525 million) of maintenance support and Rs. 110 crore (\$210 million) of non-profit assistance for development programs.

d. PL. 480 Counterpart funds. Rs. 60 crore (\$120 million) of P L 480 counterpart funds were required for the plan development program for the revised plan only. Rs. 344 crore (\$722 million) was received by Pakistan under the extended P L 480 agreement, 11 per cent of counterpart funds (Rs. 38 crore - \$80 million) was to be utilized by the United States, Rs. 65 crore (\$137 million) was transferred to the Indus Basin Fund besides the Rs. 25 crore (\$52 million) which had already been reserved

out of accumulated P L 480. In the overall second revised plan, Rs. 106 crore (\$225 million) was turned over to the Indus Basin Works through the accrual of P L 480 counterpart funds. Rs. 60 crore (\$126 million) was designed for development programs of the plan, another 160 crore rupees (\$336 million) was utilized for the works program during the span of this program.

4. Deficit finance. In the original second Five-Year Plan, the projections for deficit finance stood at 100 (crore rupees). There was no deficit finance for the revised version. It stood as 5 per cent of the original plan aggregate outlays.

Inadequacy of Financial Resources through Taxation in Pakistan. Taxation in Pakistan is neither elastic nor flexible. Rigidities ensue from the land tax revenue and other taxes on economic rents of different entities. The land revenue tax is very old and fixed. Income tax does not reach a sufficient percentage of the population. At present there is no inheritance tax. Specific assessments on the improvement of land have not been made due to different investment outlays. If elasticity is infused into the tax system so that economic rents from the

factors of production can be ploughed back into real investment outlays, taxation could very well become a larger source of funds.

Factors Responsible for Revision of the Second Five-Year Plan. The important factors which necessitated revision of the cost of plans from Rs. 1,900 crore (\$3,390 million) to Rs. 2,300 crore (\$4,830 million) were manifold. Substantial increases in both internal and external prices took place after 1959. The real cost of many projects in the original Plan were underestimated and, at the same time, some expansion relative to the physical size of the plan were visualized. The increased cost amounted to Rs. 400 (crore) (\$840 million) out of which 31 per cent was due to under provision of physical imports, 43 per cent because of increased prices and the remainder (26 per cent) represented higher physical targets. Though this caused a rise of 21 per cent in the over-all financial size of the plan, the physical targets were increased by about 5 per cent.

Besides these factors, controls on foodgrains and several other commodities were removed in 1960; coupled with some increase in international prices both for machinery and tied-aid and loans, this resulted in the financial change in requirements for the revised version of the plan. For instance, in Pakistan, the consumer

price index rose to the extent of about 9 per cent from 1959-60 to 1960-61. The tied-aid and loans led to the purchase of goods and other commodities to a specified country regardless of the availability of competitive bidding. This factor exerted adverse effects, particularly in the water and power industry and the industrial sectors which are highly dependent upon foreign imports for their effectiveness.

#### The Role of Foreign Aid, Trade, and Exchange in Financing Pakistan's Second Five-Year Plan

Introduction. The underdeveloped countries suffer from an insufficient supply of capital goods and other ancillary development goods.

Their export potentials are insufficient to pay for an adequate supply of imports to bring about the realization of their objective: an accelerated pace of industrialization. The implementation of economic plans which would help to transform their non-monetized sectors into monetized sectors could be an important prerequisite toward a break through of both economic and non-economic bottlenecks. The internal factors of production would need to be made flexible to conform to the import requirements of the industrialized economy.

Multilateralism would be a cherished goal for the attainment of required resources under competition. A

cheap supply of capital and other requirements for rapid industrialization can be possible only if foreign export potentials can be made adequate and more widely diversified. Even the terms of trade for other exports and imports of these underdeveloped economies are highly dependent upon their ability to infuse internal flexibility into the factors of production.

Internal elastic supply could be envisioned only if capacity can be kept fully utilized. A full utilization of the factors of production (particularly labor) is an important pivotal point. Introduction of new innovations, new technology, and other scientific improvements leading to a higher rate of increase in productivity are mainly dependent upon the manner in which full exploitation of potentials is engineered.

The aggregate foreign exchange earnings due to Pakistan's own export potential amounted to Rs. 1,125 crore (\$2,363 million) during the Second Five-Year Plan.<sup>18</sup> The export of raw jute rose to 4.4 million bales, jute manufactures went up to 290 tons, raw cotton to 650 thousand bales, cotton yarn to 50 million pounds, and cotton cloth to 225 million yards. Besides this, a significant increase in the amount of these manufactured goods, which



were subsidized by the export bonus scheme, was noted.

Foreign exchange expenditure towards the purchase of essential non-development goods stood at Rs. 1,375 crore (\$2,887 million) during the plan period.<sup>19</sup> There ensued a curtailment towards the importation of consumer goods due to substitution from within the economy, particularly of petroleum products and certain textile goods. Pakistan's own foreign exchange earnings were insufficient to pay for all of its non-development imports. There was a gap of Rs. 250 crore (\$525 million) which was made up through the maintenance support.

About Rs. 1,500 million of foreign exchange was available for both private and semi-public sectors.<sup>20</sup> Foreign investment outlays in oil and gas exploration and oil refining amounted to about Rs. 440 million. Besides direct foreign investments, private industry was assisted through the extension of loans from the World Bank, the Industrial Finance Corporation, International Development Association, the development loans from the monetary fund and other international agencies. These loans aggregated Rs. 500 million which were distributed under the auspices of the Pakistan Industrial Credit and Investment

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<sup>19</sup>Ibid., p. 30.

<sup>20</sup>Ibid., p. 101.

Corporation. Out of Rs. 1,500 million in foreign loans, Rs. 500 million was assigned to the semi-public sector. Rs. 1,100 million (of foreign exchange) was allocated as foreign investment towards the private sector.

Assistance under P L 480 has been over Rs. 300 million annually as food-grain aid. Assistance under the P L 480 amounted to Rs. 1,700 during the Plan; Rs. 1,000 million in the form of food-grains and 700 million in the form of non-food items. The counterpart funds which were created through the latter form of assistance were directed toward financing the local currency expenditure on the Indus Basin Replacement Works.

Counterpart Funds. According to Table IV, counterpart funds were generated through defense support aid and assistance under the U.S. P L 480. Regarding defense support, 95 per cent of the counterpart funds were by Pakistan and were available to be used subject to the approval of the United States.<sup>21</sup> The remaining 5 per cent was owned by the United States for use by United States Government agencies only. The aid under P L 480, the counterpart funds, were the property of the United States and could be released in installments in the form of loans

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<sup>21</sup>The Second Five-Year Plan, p. 36.

TABLE IV \*

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**ACCURALS AND RELEASES OF COUNTERPART FUNDS**  
**1960-61 to 1964-65 (in millions of rupees)**

Accruals	Releases
P L 665/138 Counterpart Funds (defense support) Arrivals of Commodity Aid ..... 2500	P L 665/138 Counterpart Funds (defense support) Induction of military aid ..... 625
Customs on Commodity Aid 500	Five per cent of ICA expenditure ..... 125
P L 480 Counterpart Funds Foodgrains ..... 1,000	Releases for Development projects..... 1,250
Non-food Items ..... 700	P L 480 Counterpart Funds U.S. Uses..... 250
	Releases for Development Projects..... 750
	Releases for Indus Basin Replacement Works ..... 700
Total ..... 4,700	Total ..... 4,700

\* Source: Second Five-Year Plan of Pakistan, p.37

and grants to Pakistan for specific development projects. The accruals of counterpart funds must be matched by simultaneous releases so that expansionary or contractionary

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Utilization of counterpart funds from commodity aid (U.S. P L 665/138 and foodgrains aid) (P L 480) is finalized subject to agreement between the United States and Pakistan.

influences from this source could be neutralized for the maintenance of stability in the economic system. If formal releases lag behind (or exceed) accruals in a particular year, corresponding borrowings from (or payment of debts to) the State Bank must be synchronized for the maintenance of balance between the inflow and outflow of cash. The aggregate accrual of counterpart funds amounted to Rs. 4,700 million, out of which Rs. 1,000 million were reserved for both the United States uses and for the induction of military aid. Rs. 700 million were allocated to cover the local currency expenditure on the Indus Basin Replacement Works. The remaining balance of 3,000 million were set aside for development projects.

There are projects, particularly in the fields of health, education and social welfare, which are important prerequisites for the continuous rate of economic growth, but do not qualify for project aid. It is almost impossible to obtain certain developmental imports such as fertilizers, plant protection equipment, pesticides, small machinery and tools, iron and steel products, under project aid. The public sector received aid of Rs. 4,000 million which was not tied to any particular project.<sup>23</sup> Presently, defense support from the United States and some amount of

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<sup>23</sup>

The Revised Second Five-Year Plan, p. 100.

commodity aid from the Colombo Plan countries form the only aid that is not tied to a particular project. The real value of aid is depreciated if it is tied to be purchased from specific countries. When aid is tied there is not always a possibility of obtaining the required imports at competitive prices. This leads to higher costs in terms of monetary purchasing prices.

Negotiations for aid, signing of project agreements, contracting for engineering services, and the ordering of equipment in accordance with the conditions laid down by the aid giving agencies, are time consuming procedures. Consequently, the imports through aid, do not always materialize in the year in which the aid is assigned to a particular project. Ordinarily it takes about two years before aid operations can be implemented for certain projects.

### Summary and Conclusions

Along with the Second Five-Year Plan, two programmes namely: The Indus Basin Replacement Works and the Works Programme were carried out. Financing of the Revised Second Five-Year Plan was carried out mostly through foreign aid (to the extent of 50 per cent of the total--resources, amounting to 23,000 million rupees). The Indus Basin Replacement Works cost 3,000 million rupees and the

Works Program cost 1,600 million rupees (both financed solely through foreign real resources through the availability of foreign real investment outlets).

Internal real net savings could have been raised to a great extent by imparting greater flexibility and elasticity in the tax system. Economic rent from various factors of production could be mobilized for real investment expenditures so that internal factors of production could not only be made mobile and flexible but the capacity of the economy could be utilized to an optimum level through their full utilization.

These domestic resources would then be supplemented by large imports of foreign capital, i.e., grants, loans, and private foreign investment. Capital imports would be concentrated in the early period of the development effort so that by the end of the prospective plan in 1985, we would witness the elimination of dependence on foreign assistance.

## **CHAPTER V**

### **THE ROLE OF MONETARY AND FISCAL INSTITUTIONS AND POLICIES**

#### **Purpose and Organization**

The role of monetary and fiscal institutions and policies is discussed in this chapter. Their effective utilization can enhance productivity of the economy. The money supply should be elastic in nature, so as to attain a continuous rate of economic growth with stability of the price level. The expansion of commercial banks, along with specialized credit institutions, should be handled in such a way that optimum productivity can be raised in the long run without involving any inflationary spiral. The non-monetized sector, particularly the agricultural sector, must be financed to an adequate level for the attainment of a self-cumulative rate of economic growth.

The role of fiscal management should be such that an elastic system of taxation, debt management and governmental expenditure could be introduced. Economic rent through new and various taxation could be manipulated in such a way that an optimum rate of real investment expenditures can be attained. The coordination and integration of both fiscal

and monetary measures should be such as to procure a stable, continuous rate of capital formation sufficient to counterbalance the rate of increase in population growth.

The organization of this chapter is as follows: It is divided into five parts. The first part discusses introduction of the proper utilization of both monetary and fiscal operations.

The second part throws some light on money, output, and the price level during the 1950's. In the under-developed economies, the capacity to produce sufficient consumers' goods and producers' goods in the short run is limited as compared to the increasing level of real investment expenditures for higher economic productivity.

The third part discusses the rationality of integration of both fiscal and monetary policies for stable economic growth. The fourth part emphasizes the introduction of credit policy and financial institutions for stability and growth. The rate of aggregative productivity in the long run should be commensurate with the supply of credit and expenditures for a socially desirable rate of economic growth. The elastic supply of credit towards the non-monetized sector—particularly the agricultural sector, will help to build a sound foundation upon which long-run growth can be attained.



The fifth part emphasizes the introduction of not only an elastic tax policy but new taxes such as an inheritance tax and betterment specific taxation so that sufficient economic rent from all the factors of production can be mobilized towards real investment expenditures for a higher rate of economic productivity.

### Introduction

"In a country with well developed banking and credit institutions, and a capital market, regulation of the banking systems by the Central Bank plus the operations of the bank in the bond market may constitute a control mechanism of delicacy and power. But if there is no bond market and little use of bank credit, a quite different set of controls is necessary. Similarly, the tax and fiscal policies or foreign exchange controls appropriate to an economy with a fairly elaborate complex of financial records may be largely irrelevant to a simpler economy." <sup>24</sup>

During the second Five-Year Plan, emphasis was placed on the utilization of indirect controls instead of the extensive use of direct controls. Both monetary and fiscal measures were relied upon for the regulation of the economy. Fiscal measures such as taxation, government expenditures, and debt management, along with monetary

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<sup>24</sup>Hagen, op.cit., p. 332.

measures, such as open market operations, changes in reserve ratios, and variations in discount rates, can lead to changes in the pattern of production, consumption, investment, real saving, and international trade. These measures can be utilized to help neutralize inflationary pressures and to mobilize real resources towards economic development. Higher rates of taxation, accompanied by tightening of credit availability, can be a major factor in neutralizing economic cycles for a continuous and stable rate of economic growth. Higher rates of taxation, coupled with higher rates of interest, can also be used to encourage real savings and selectivity in the economic use of real capital investment.

#### Money, Output, and the Price Level During the 1950's

The money supply has increased at an average rate of about 10 percent annually for the last ten years;<sup>25</sup> while gross national product went up by about 3 percent annually. (See Tables I and II) The normal presumption would be that the results would be inflationary. But this analysis overlooks a substantial increase in the demand for liquidity which can occur in a developing economy without a correlative rise in either output or the price level

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The Second Five-Year Plan of Pakistan, p.57.

in the short run. In Pakistan, there was a rise in the money supply from about 15 per cent of gross national product in 1949-1950 to over 20 per cent by 1959-1960.<sup>26</sup> Also, an increasing supply of goods and services through the provision of foreign assistance helped in absorbing a part of the rise in money supply. The general price index (Table III) will help to illustrate.

In West Pakistan there was a substantial increase in the price level in 1952-1953. Then, during 1954-1955, prices fell almost 20 per cent. This was due to an exceptionally good crop; wheat production had increased substantially compared to the following year. Consequently, wheat prices went down to an extremely low level of 8/15/- per pound.<sup>27</sup>

In East Pakistan prices declined by almost 40 per cent during 1951-1952 to 1954-1955, but afterwards rose steadily.<sup>28</sup> These price variations are explained largely by fluctuations in the supply of rice on the free market and the growing pressure of monetary demand. Prices of similar goods had generally been higher in East Pakistan as compared to West Pakistan. This could be partly explained by lack of sufficient means of communication and

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<sup>26</sup>Ibid., p. 58.

<sup>27</sup>Ibid., p. 59.

<sup>28</sup>Ibid.

TABLE I

## MONEY SUPPLY \*

Year	Currency	Deposits	Deposits	Total	Index of velocity of cir- culation of bank Deposits
1949-50	1,750	913	49	2,712	100
1950-51	1,961	976	68	3,005	100
1951-52	2,275	1,148	42	3,465	102
1952-53	2,164	1,049	35	3,248	102
1953-54	2,344	1,182	24	3,550	101
1954-55	2,519	1,203	43	3,765	98
1955-56	2,899	1,333	47	4,279	106
1956-57	3,340	1,408	80	4,824	107
1957-58	3,517	1,602	75	5,194	101
1958-59	5,596	1,761	74	5,431	100

\* Source: Second Five Year Revised Plan, Page 57.

TABLE II

## GROSS NATIONAL PRODUCT

Year (GNP) (a)

1949-50	17,544
1950-51	18,327
1951-52	18,303
1952-53	19,074
1953-54	20,508
1954-55	20,913
1955-56	20,840
1956-57	22,186
1957-58	22,200
1958-59	22,277

(a) In 1949-50 to 1952-53 average prices.

TABLE III

GENERAL PRICE INDEX 1951-52 to 1958-59 \*

(Base 1951-52 = 100)

	West Pakistan	East Pakistan	All Pakistan
1951-52 .....	100	100	100
1952-53 .....	111	96	104
1953-54 .....	96	78	87
1954-55 .....	80	61	71
1955-56 .....	92	83	88
1956-57 .....	112	84	98
1957-58 .....	108	97	102
1958-59 .....	111	117	114

\* Source: The Revised Five-Year Plan, p. 58

shipment between the two regions. The food-grain supply is an important factor in the determination of the general price level in East Pakistan. This region of the country is less diversified than West Pakistan, where patterns of production are more diversified due to the rising availability of the supply of manufactured goods from domestic industries.

The money supply was about Rs. 4,000 million toward the end of 1955.<sup>29</sup> Banks had excess reserves of approximately Rs. 150 million by October, 1959; the position

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<sup>29</sup>

Ibid., p. 60.

became normal afterward and the excess reserves disappeared. There was an excess liquidity in the system because fluctuations on the stock exchange had been oversubscribed many times. Speculative tendencies in the market and easy access to bank credit had been responsible for encouraging this trend. To neutralize it, restrictions were placed on stock market margins required by the banks, against security of old and new shares. Time deposits were somewhat swollen and this helped toward higher savings. Excess liquidity may be frozen simply by a change in the reserve requirements of the commercial banks. The prevalent statutory reserves were 2 per cent of time deposits and 5 per cent of demand deposits during the Plan period.<sup>30</sup> Requirements for prior deposits on import licenses or through funding some part of the public debt and through stabilization program of substantial imports for a limited time at high surcharges could have been stabilized. However, price increases consequent upon the lifting of controls on foodgrains helped in absorbing a part of excess liquidity.

#### Fiscal and Monetary Policy for Economic Stability and Growth

"Appropriate economic policies must be pursued if the Plan is to be fully implemented. It is intended to move away from extensive use of direct

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<sup>30</sup>Ibid., p. 61.

controls, which has tended to retard the pace of development, and to rely mainly on fiscal and monetary measures to regulate the economy. Fiscal measures can exert a powerful influence on the pattern of production, consumption, investment, savings and international trade. They can also be used to control possible inflationary pressures and to mobilize resources for development by augmenting government revenues."<sup>31</sup>

Real investment expenditure in the development program was expected to affect substantially the utilization of the real resources of the country. Because there still are unused and immobilized resources, increased expenditures may not lead to an inflationary spiral in the short run. If increases in the supply of goods and services lag behind the increasing level of investment expenditure, however, the danger of inflation can not be ignored. A good or bad harvest can profoundly affect the stability of the economy. (Because of this, incidentally, it was thought advisable to devise a reliable and comprehensive index of internal price movements dependent upon up-to-date data.)

A substantial increase in prices leading to a long term trend would necessitate adjustments in the fiscal operations of the government sector. The first objective should be the raising of taxes to combat inflation; if this proves ineffective, curtailment of development

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<sup>31</sup>The Revised Second Five-Year Plan, p. 47.

expenditures, of the government sector particularly, should be ordered.

Annual development programs should be consistent in relation to availability of resources and the composition of the development program. For greater efficiency and consistency, all adjustments should be made in time. It takes some time for the development programs to be adjusted and for the operations of the fiscal policy to be implemented. An increase in excise taxes is probably the most effective way to curtail demand during an inflationary spiral. Excise taxes might lead to an increase in the prices of the goods taxed, but this rise would be far outweighed by the deflationary effect brought about by the transfer of this tax money to the government sector.

Also, during an inflationary period, money could be controlled by making credit more expensive. The State Bank could raise the bank rate and thereby discourage borrowing. It could also raise reserve requirements in order to neutralize the surplus reserves in the banking system. Introduction of prior deposits on applications for import licenses could be utilized in mopping up excess liquidity. However, in order to exploit full capacity of the economy, credit controls should be made elastic for greater flexibility of the factors of production.



Special measures were implemented for offsetting the instability due to harvest fluctuations. The government, in cooperation with the United States, decided to keep wheat prices within specified limits by establishing a buffer stockpile of wheat. This policy helped to insure a great degree of stability in the cost of living in West Pakistan. A buffer stock could not be established in East Pakistan because of the lack of elastic supply; however, efforts were directed toward the free flow of goods from West to East Pakistan to offset inflationary pressures there. It was suggested to set aside price controls whenever possible because they are not only difficult to administer but costly as well, and may frequently lead to the discouragement of production. Goods included were sugar, tea, wheat and rice and certain types of cloth, of which the given supply needed to be brought into equilibrium at noninflationary prices. During the Plan period, five major steps were devised as anti-inflationary policy. Heavy emphasis was placed on the maintenance of adequate reserves of foodgrains. The use of taxation to absorb excessive purchasing power was considered highly effective, and a greater usage of monetary policy, inclusive of the manipulation of interest rates and credit policy that previously existed, was stressed. Increased efforts toward a more elastic supply of goods and services

commensurate with the increasing level of income were also made. Price controls, imposed on a very few essential commodities and for very limited periods, were considered a last resort.

The development program had been drawn up in terms of prices prevailing in 1959.<sup>32</sup> During the second Five Year Plan prices rose, resulting in higher costs for the inputs which were used in the development plan. Consequently, expenditures rose in physical terms. Receipts from some taxes also increased and specific taxes were raised for the maintenance of their real incidence. Charges of railways, post office, and various other public corporations were increased commensurate with rising costs. Particular attention was directed to making sufficient provision for depreciation. A more detailed explanation is found in Table IV on the following page.

#### Credit Policy and Financial Institutions for Stability and Growth

Credit Policy. Commercial Banks, specialized credit institutions, and the stock exchange, were responsible for the provision of Rs. 1,650 of credit during the Plan period.<sup>33</sup> The two first mentioned institutions created credit mainly for the private sector. Provision

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<sup>32</sup>Ibid., p. 67.      <sup>33</sup>Ibid., p. 69.

TABLE IV  
ADJUSTMENTS IN PRICES AND PHYSICAL TARGETS\*

Field of Development	Original Plan Allocation	Rev. Plan Allocation	Increase in Plan Allocation	Prov. of Physical Inputs	Price Increase	Increase in Physical Target
Agriculture.....	302	342	40	7	6	27
Water & Power.....	339	439	100	49	51	--
Industry.....	405	512	107	40	64	3
Fuels & Minerals..	85	100	15	--	5	10
Transport & Communication.....	335	405	70	11	23	36
Housing & Settlements.....	284	341	57	10	20	27
Education & Training.....	97	105	8	6	2	--
Health, Manpower & Social Welfare....	53	56	3	2	1	--
Total:	1,900	2,300	400	125	172	103

\*Source: Table III, Revised Second Five-Year Plan, p. 13.

of additional credit amounting to Rs. 154 million annually was made during 1955-56 to 1958-59, of which 94 million was created by commercial banks and the remainder by specialized institutions. These institutions were important factors in meeting the credit requirements of the economy. Industry secured more than 40 per cent of this additional credit,<sup>34</sup> while agriculture drew about 25 per cent from specialized credit institutions such as the Agricultural Development Finance Corporation and the cooperatives. The construction and transport sectors received about Rs. 45 million for private construction objectives. The following table shows the position of these credit creating banks. (Table V, Chapter V.)

The government decided against undertaking any deficit financing during 1960-65. This was under the impression that the money supply (Rs. 150 crore or \$315 million) could be expanded without any serious danger of inflation.<sup>35</sup> This assumption was based upon the hope that national income would go up by about 24 per cent. Consequently, net bank credit of about Rs. 150 (\$315) could be extended to the private sector and still be within "safe" limits of price stability. Private credit increased to the extent of Rs. 77 crore (\$162 million) during 1959-60 and 1960-61. However, this was offset by the increase in

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<sup>34</sup>Ibid.      <sup>35</sup>Ibid., p. 32.

TABLE V  
SOURCES AND USES OF ADDITIONAL CREDIT  
1955-56 to 1958-59\*  
(in millions of rupees)

	1955-56	1956-57	1957-58	1958-59	Total	Annual Average
<b>Sources:</b>						
Commercial Banks.....	59	194	83	41	377	94
Specialized Credit Institutions..	56	56	65	64	241	60
<b>Total:</b>	<b>115</b>	<b>250</b>	<b>148</b>	<b>105</b>	<b>618</b>	<b>154</b>
<b>Uses:</b>						
Agri. ....	29	24	52	64	169	42
Indus. ....	103	60	97	-3	257	64
Trans. ....	-7	1	9	-4	-1	0
Const. ....	6	3	24	13	46	11
Other Services.....	-16	162	-34	35	147	37
<b>Total:</b>	<b>115</b>	<b>250</b>	<b>148</b>	<b>105</b>	<b>618</b>	<b>154</b>

\*Source: Revised Second Five-Year Plan, p. 69.

time deposits to the extent of Rs. 50 crore (\$105 million). A net credit creation of Rs. 27 crore (\$57 million) was provided for the private sector.<sup>36</sup> Expansion in the private sector was due to: (1) decontrol of foodgrains, (2) liberalization of imports, (3) rise in jute prices, and (4) expenditures in the interest of fast industrialization, consequent upon relaxation of economic controls.

In the event there had arisen a need for expansion of credit creation by the commercial banks, the State Bank could have bought up government securities and through other monetary measures increased the reserves of these banks.

### Financial Institutions

Commercial Banks. Commercial banks provided additional credit to the extent of Rs. 700 during the Plan period.<sup>37</sup> Outstanding loans and reserves by the commercial banks had risen from Rs. 723 million in June, 1955 to Rs. 1,100 million by June, 1959, thereby leading to an average annual increase of about 12 per cent. There arose some special problems in the field of commercial banking; sectoral distribution of bank credit was overwhelmingly included toward industry and commerce; bank credit was concentrated in the hands of a few individuals and firms.

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<sup>36</sup>Ibid., p. 33.      <sup>37</sup>Ibid., p. 70.

For instance, on March 31, 1959, 63 per cent of the total bank credit was allocated to only 222 accounts in the form of advances of Rs. 1 million or above; advances extended to borrowers of small means was about 6 per cent of total credit; Pakistan had but one bank office for every 150,000 population.<sup>38</sup> Besides this, 157 out of a total 247 important marketing centers had no banking facilities whatsoever.

It was felt imperative that the State Bank be able to infuse flexibility and a more elastic supply of credit through the commercial banks, particularly to the small entrepreneur. Under favorable economic conditions, the small entrepreneur helps to enhance the rate of productivity in the economic system. There had been an increase in the number of branches from 246 in 1954 to 372 in 1959.<sup>39</sup> This helped, to some extent, to satisfy the increasing demand for more flexible facilities for a higher rate of development expenditures.

Specialized Credit Institutions.<sup>40</sup> For the fulfillment of the special credit needs of certain sectors, a number of finance corporations have been established. These finance corporations include the Agricultural Development Finance Corporation (ADFL), the Agricultural Bank,

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<sup>38</sup>Ibid., p. 71.    <sup>39</sup>Ibid.    <sup>40</sup>Ibid.

the Pakistan Industrial Finance Corporation (PIFCO), the Pakistan Industrial Credit and Investment Corporation (PICIC), and the House Building Finance Corporation (HBFC). Besides these, cooperative societies and banks have been meeting the credit requirements of the agricultural sector. These corporations have offered some services that were not provided by the commercial banks (which included borrowing on short-term basis), namely, medium and long-term credit for the industrial sector; provision of credit facilities for those trades and industries where specialized knowledge and skills were the important prerequisite; and, finally, accommodating enterprises where higher risks prevailed. Some of these corporations had been extending credit to a few established concerns rather than to new enterprises. On the whole, these corporations performed an intermediary service for the distribution of government credit to various sectors at subsidized rates. Loans through credit creation by these institutions are shown in Table VI, this chapter.

Agricultural Development Finance Corporation and Agricultural Bank. The additional credit created by ADFC did not exceed rupees 6 million per annum.<sup>41</sup> This was insufficient to meet the requirements of agricultural

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<sup>41</sup>Ibid., p. 73.



credit. These two institutions had been entrusted with similar responsibility in different geographic jurisdictions. It was thought feasible to merge the two into a single institution for meeting credit demands of the agricultural sector. It had been hoped that around Rs. 150 million would be invested in this sector through the amalgamated institution. Savings would be mobilized either in the form of deposits or through flotation of equity shares. Sufficient real savings could be mobilized from the market only if optimum deposit rates were offered. The prevailing leading rate of 5 per cent had to be revised upward to achieve this objective.

Cooperatives. The additional loans created by cooperative societies had averaged in the neighborhood of Rs. 28 million per annum.<sup>42</sup> It was thought essential that the rate of lending to the agricultural sector by these cooperatives be expanded at least to an additional amount of Rs. 200 million during the Plan period.

Pakistan Industrial Finance Corporation. PIFCO had been lending about Rs. 10 million per annum.<sup>43</sup> About 66 per cent of its resources had been channeled to the textile industry. Its loans had been concentrated in a limited number of borrowers. It had been playing the role

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<sup>42</sup>Ibid.      <sup>43</sup>Ibid.

**TABLE VI**  
**LOANS BY SPECIALIZED CREDIT INSTITUTIONS\***  
**1960-61 to 1964-65**  
**(in millions of rupees)**

	<u>1955</u> <u>1956</u>	<u>1956</u> <u>1957</u>	<u>1957</u> <u>1958</u>	<u>1958</u> <u>1959</u>	Annual Average 1955-56 1958-59	Average Second	Total Second
<b>ADFC<sup>a</sup></b>	2	3	7	13	6		
<b>Agri. Bank Corp.</b>	(a)	(a)	(a)	3	(a)	30	150
<b>Coop.</b>	27	22	33	30	28	40	200
<b>PIFCO<sup>b</sup></b>	13	19	10	9	12	20	100(c)
<b>PICIC<sup>c</sup></b>	--	--	--	--	--	--	--
<b>HBFC<sup>d</sup></b>	14	12	15	9	13	40	200
<b>Total:</b>	56	56	65	64	60(b)	130	650

<sup>a</sup>Agricultural Development Finance Corporation.

<sup>b</sup>Pakistan Industrial Finance Corporation.

<sup>c</sup>Pakistan Industrial Credit and Investment Corporation.

<sup>d</sup>House Building Finance Corporation.

(a) Began operation in 1959.

(b) Excluding local currency loans by PICIC.

(c) PIFCO and PICIC provided total additional rupee finance amounting to Rs. 200 million; including Rs. 100 million borrowed by PIFCO for commercial banks. As this amount has been included in finance provided by the commercial banks, it has been excluded from this table to prevent duplicate counting.

\*Source: Revised Second Five-Year Plan, p.72.

of an intermediary between the banking system and the industrial borrowers and had obtained loans on a short-term basis for the provision of some long and medium-term loans. It was felt that it should become more of a development bank than an exclusive mortgage bank; it should lend not only against security of existing assets but should also provide credit against prospective assets, thereby encouraging the initiative and growth of new enterprise. Subscription to the equity of private limited companies should also be initiated. Since there had been no adequate credit facilities extended to the Inland Water Transport and Mining sectors, this corporation should endeavor to create credit facilities for a considerable expansion of real investment expenditures in these sectors. PIFCO had lent about Rs. 150 million during the Plan;<sup>44</sup> it obtained Rs. 80 million from the government, about Rs. 50 million was advanced by the banking system and the balance was obtained through deposits or equity finance.

Pakistan Industrial Credit and Investment Corporation. The primary role of PICIC has been the provision of foreign exchange to private industry secured from the Development Loan Fund, World Bank, and other sources. It had been acting as an underwriter for foreign loans so

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<sup>44</sup>Ibid.

that the inflow of foreign investment to private industry could be stimulated. Its current scale of operations involved about Rs. 50 million annually.<sup>45</sup>

House Building Finance Corporation. This corporation was set up in 1952, and has been advancing credit to the extent of Rs. 10-15 million per year. Its maximum loan ceiling had been Rs. 40,000 for individuals with a maximum time limit for repayment of the loans set at 15 years;<sup>46</sup> the interest rate was 6 per cent. Borrowers had been subject to initial investment of 20 per cent of the estimated cost of the building and land. The corporation had been wholly financed by the government sector and had loaned credit beyond its paid up capital to the extent of Rs. 50 million. HBFC had disbursed credit amounting to approximately Rs. 200 million for the construction of low cost housing, acquiring Rs. 120 million from the government sector and the balance of Rs. 80 million from a higher level of deposits or equity finance.

Stock Exchange. Since establishment of the Karachi Stock Exchange in 1949, there has been an increase in investorships from 9 to 167 with total listed shares amounting to 71 during the second Plan period. The Stock Exchange started its operations in 1956 with Rs. 100 millions<sup>47</sup> advanced out of total capital of Rs. 230 millions

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<sup>45</sup>Ibid., p. 74.    <sup>46</sup>Ibid.    <sup>47</sup>Ibid.

subscribed by new companies from 1955 to 1959. The Stock Exchange had been unable to realize sufficient real savings from the public. There had been a lack of well organized stock exchanges in places other than Karachi; most public limited companies had not availed themselves of the facilities offered by the stock exchange in the flotation of securities for raising needed funds. Both the Pakistan Industrial Credit and Investment Corporation and the Pakistan Industrial Finance Corporation had been authorized to underwrite the issue of stocks and shares and to sponsor the provision of capital to industrial companies through the intermediary of the stock exchange. This had affected the availability of an elastic supply of capital for the optimum expansion of the industrial sector within a given span of time. Small investors could be induced to invest their real savings in securities through the supply of shares in small amounts and through the provision of a simplification of the operations involved, as well as the ready marketability of the shares.

The development of an effective marketability of government securities for non-institutional investors had not been provided by the stock exchange. A yield of 4 per cent on government securities had been substantially lower as compared to yield on industrial shares amounting

to 6.5 per cent.<sup>48</sup> A lack of marketability of government securities existed because the State Bank of Pakistan had been selling government securities without giving serious consideration to the prevalence of a tightness of credit and, consequently, the increase on the call rate for money for non-institutional investors. Private industry had been able to mobilize about Rs. 300 million through the stock exchange during the Plan period.<sup>49</sup>

Insurance. Insurance companies generally have been able to mobilize substantial amounts of real savings through encouraging the saving habit among the people. In Pakistan, insurance had been unable to contribute materially toward a higher rate of capital formation. The assets of insurance companies had amounted to about Rs. 200 million in 1957.<sup>50</sup> The average investment by these companies had been around Rs. 15-20 million per annum. These companies had been conducting their business primarily with insurance against fire, marine and accident risks, and a greater percentage of premium income had been drawn from claims and operating expenses. The cost of collection had gone up as high as 40 to 50 per cent.<sup>51</sup>

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<sup>48</sup>Ibid., p. 75.

<sup>49</sup>Ibid., p. 75.

<sup>50</sup>Ibid.

<sup>51</sup>Ibid., p. 76.

### Tax Policy for Economic Growth

"The tax system needs to be directed increasingly towards meeting the long-term needs of development. This will imply a greater use of taxes and subsidies to secure a desirable allocation of resources, instead of relying on a multiplicity of direct controls; the use of taxation as a means to control inflationary or deflationary tendencies; and the raising of more revenue to provide the means of development. The tax system will also need to be revised to broaden its coverage, make it more flexible, rationalize its incidence, and ensure the best balance between direct and indirect taxes."<sup>52</sup>

Tax policy should be formulated in such a way that the allocation of real resources can be mobilized for economic development according to Plan priorities. Tax systems should be framed so that an elastic increase in the public revenues will accompany the rate of increase in the national income. The base rate on consumption goods should be raised on luxury goods. However, direct taxes should be levied in such manner that they will not adversely affect the incentive to work and save. Overall tax policy should be oriented toward diverting higher incomes into real savings and investment rather than go into consumption expenditures. "Disguised" taxation, such as the compulsory accrual of foodgrains at prescribed prices, adversely affects the incentive to produce and invest. Therefore, the tax policy should help coordinate the broader objectives of the development policy of the country.

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<sup>52</sup>Second Five-Year Plan, op. cit., p. 49.

### Sources of Additional Taxation

Import Duties. Imports are subject to direct controls. These controls have helped to restrict imports and conserve foreign exchange, but they have often been responsible for shortages of spare parts, key raw materials, and substantial unearned profits for the importers. Generally, importers had been able to charge higher prices for those imports whose supply was rationed. Imposition of a system of import surcharges high enough to equilibrate the given demand and supply on the market would work to good advantage.

Commercial imports were short by about Rs. 800 million and had gone up during the five years of the Plan. Surcharge rates could be adjusted downward on essentials like drugs and medicines, with more than 100 per cent being collected for luxury goods. If the average surcharge rates had amounted to 20 per cent, total accruals from this tax could have yielded about Rs. 1000 millions during the Plan period.<sup>53</sup>

Export Duties. The export bonus scheme stimulated the incentive for a higher amount of export of manufactured goods. This suggests that a successful export drive can be continued only if an elastic supply of exportable goods can be produced at home. In order to adjust export

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<sup>53</sup>Ibid., p. 51.



duties, the effect on internal prices, the loss of subsidies for cotton and jute manufactures, and the problem of a transfer of income from non-agricultural to the agricultural sector will have to be analyzed. The government had drawn about Rs. 700 million from export duties at the prevailing rate.<sup>54</sup>

Land Taxes. The low yield from land tax revenue in West Pakistan is due to several reasons. There was involved a long period—some thirty to forty years—of settlement, with a maximum ceiling of 25 per cent on the enhancement of land revenue at the time of settlement.<sup>55</sup> Revenue from agricultural taxation should be made elastic to correspond with the growth of output and prices and, at the same time, it should not adversely affect the incentive to produce and to make real investment expenditures. Water rates had been the same generally over the past thirty years; in West Pakistan the government had been unable to cover the cost of providing water due to low water rates. These rates must be raised sufficiently to run this department on a commercial basis. Imposition of betterment taxes as well as the extension of the estate duty to agricultural property could help to raise additional revenue. A part of economic rent could have been

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<sup>54</sup>Ibid., p. 52.      <sup>55</sup>Ibid., p. 54

deducted from the prices on land which had received improved irrigation facilities consequent upon the construction of new barrages, through utilization of betterment levies. The levying of death duties has been responsible in some countries for reducing the extreme inequalities of income through gradual liquidation and distribution of large reclamation of wealth, including land ownership. This has led to a higher rate of economic productivity and net savings in the long run. Additional taxation amounting to approximately Rs. 500 million could be drawn from the agricultural sector through such measures during the next Plan.<sup>56</sup>

Direct Taxation. Direct taxation (income tax, corporation taxes and property taxes), as well as tax concessions, should be re-evaluated in the light of the objective of long-run growth. Tax concessions could be used to encourage a higher rate of reinvestment of profits. Taxes on property by various agencies (the central government, provincial governments and municipalities) should be amalgamated so that the combined burden of the incidence of property taxes can be reduced. The introduction of a capital gains tax should be given serious consideration. More detailed information concerning these taxes is given in Table VII, Chapter V.

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<sup>56</sup>Ibid., p. 55.

**TABLE VII**  
**ACTUAL AND EXPECTED GROWTH OF TAX REVENUE**  
**1949-50 to 1964-65**  
**(Consolidated Central and Provincial Receipts)**

In million rupees.				
	1949-50 (actual)	1953-54 (actual)	1959-60 (Budget Est.)	1964-65* {Projections} (a) (b)
<b>Composition of tax receipts;</b>				
<b>Income &amp; Corp. Tax.....</b>	115	212	265(c)	400
<b>Land Revenue...</b>	134	178	295	320
<b>Customs.....</b>	463	401	490	650
<b>Excise Duties..</b>	99	221	310	390
<b>Sales Tax.....</b>	149	158	285	390
<b>Misc.....</b>	108	76	205	220
<b>Total Tax Revenue:</b>	1,068	1,246	1,850	2,270 2,600
<b>Dist. between Dir. &amp; Indir. Taxes:</b>				
Direct.....	269	407	602	760
Indirect.....	799	839	1,248	1,510
<b>Ratio of Dir. Taxes to Total Tax.....</b>	25%	33%	33%	33%
<b>Tax Revenue as Percent- age of GNP in current prices.....</b>	6.1	6.9	7.3	7.4 8.5
(a) Excluding additional taxation during second Plan period.				
(b) Including additional taxation during " " " "				
(c) Excluding extraordinary collections of tax arrears.				

\*Source: Revised Second Five-Year Plan, p. 56.

### Summary and Conclusion

Under the Second Five-Year Plan, monetary and fiscal measures were stressed to attain a stable rate of economic growth instead of implementation of direct measures such as rationing and licensing of a quota system during this Second Plan.

The rate of increase in the money supply was higher than the rate of increase in the gross national product. There occurred an inflationary spiral because the supply of goods lagged behind the generated income by the increased real investment expenditures. The coordination of both fiscal and monetary measures along with an adequate supply of food was utilized as an anti-inflationary step.

Commercial banks and other specialized credit institutions extended a greater percentage of credit to the industrial sector as compared to the agricultural sector. Small scale borrowers were discriminated against in the cost of borrowing as against the large-scale borrowers. The mobilization of savings from non-institutional sectors could have been higher had the interest rate offered them been proportionately higher as compared to the prevailing rate of interest.

The tax policy for economic growth should be made elastic by increasing the rate of national income.

Incentives can be provided for induced real investment expenditure towards economic growth. Death duties, betterment taxes, as well as the extension of the estate duty, could be levied and thus raise capital formation and, at the same time, impart a higher rate of economic growth. Imposition of taxes on economic rents of various factors of production could be directed towards enhancing real investment expenditures without adversely affecting the incentive to work, to save, to invest and take risks in various economic enterprises.

**CHAPTER VI**  
**HUMAN, ADMINISTRATIVE, AND ORGANIZATIONAL**  
**DIMENSIONS OF DEVELOPMENTAL PLANNING**  
**IN PAKISTAN**

**Purpose and Organization**

This chapter stresses human, administrative, and organizational dimension of developmental planning in Pakistan through the optimum exploitation and utilization of the factors of production, particularly labor. A full utilization and exploitation of human potentials, particularly, leads to a higher rate of economic productivity in the long run. The flexibility and mobility of the factors of production to its full capacity would be extremely productive for a self-sustained rate of economic growth. The effective participation of the "grass roots," combined with decentralization commensurate with ability, should lead to higher economic efficiency and stability of economic growth.

In underdeveloped economies such as Pakistan, a long run growth model is preferred to a short run growth model where overhead capital investments are preferred to

social welfare programs. An optimal combination of direct controls and indirect controls through monetary and fiscal operations would be an instrument towards an induced higher rate of technology, innovations and new scientific inventions. Statistical information concerning macro and micro economic sectors would be an important pre-requisite when the capacity of the economy is to be utilized to the fullest extent. The non-monetized sectors, particularly the agricultural sector, has to be transformed into a monetized sector so that indirect controls can be made effective according to a desirable alternative--priority of the allocation of the scarce resources. If full utilization of the factors of production both in the short and long run are implemented, a desirable rate of economic growth can be visualized.

### Introduction

Leadership in a democracy, with special reference to the productivity accruals from the utilization of the scarce resources of the government personnel, assumes a task of gigantic stature. The rate of growth in productivity possible if an optimal rate of combination of the private and government sectors can be achieved, depends greatly upon effective leadership. In order to bolster the dynamics of free enterprise, the government sector

must try not to compete with the private sector in the allocation of the scarce resources of the economy. The government must be able to break through economic and non-economic bottlenecks so that the majority of free enterprises can be strengthened.

To help to stabilize and ensure increasing productivity, effective participation of the "grass roots," must be secured. This would lead to coordination, unification and integration of voluntary efforts for the achievement of a desirable rate of economic growth. Leadership in a democracy should be able to bring about the introduction of formal and informal organization both voluntary and via laws and regulations. Economies of scale should be derived from these organizations, dependent, of course, upon the division of labor and specialization. These organizations are prone to become rigid and replete with red-tape. It is the business of leadership to infuse flexibility and mobility into them by imparting new ideas, innovations and new technology. In this way productivity can reach and maintain a desirable level. Full utilization of the factors of production between the government and the private sectors at a point where marginal social benefit and marginal social cost are in equilibrium would contribute to an optimum rate of economic growth.



A long-run growth model must be preferred over short run models. The factors of production must be made flexible and mobile to obtain a self-sustained economic growth level in the long run. An optimum level of effective information regarding economic plans, policies and objectives pursued by political leaders must be successfully communicated to the "grass roots." Allocation of scarce resources must be assigned to competing alternative priorities in such a way that the optimum rate of real investment expenditures will be come available for the implementation of these economic plans; decentralization commensurate with respective ability would extremely productive. An optimum organization, with the greatest degree of decentralization possible, should be the cherished goal of leadership.

Division of labor and specialization are factors to be used in making available the economies of scale required for the goals to be achieved. In modern organizations, inter-dependence is highly centralized. There is a never-ending clash between authority and corresponding ability. Bureaucrats often seek to misuse their authority. Innovations and new technology are often discouraged because their introduction might serve to curb their authority to issue orders. Bureaucrats are in control of the channels of communication; and unless these channels are

open in both directions, productivity is certain to suffer.

An optimum organization with decentralization would help in utilizing authority commensurate with ability. A higher rate of economic growth would follow because of encouragement toward adoption of innovations, technology, and automation. Such an organization, with decentralized power for the utilization of specialists, would infuse flexibility; and this flexibility would bring new ideas and new innovations which are responsible for a higher rate of capital formation in the economic system. An optimal rate of combination between the government and the private sectors and an optimum organization with decentralization would help to achieve the socially desirable rate of economic growth.

This Chapter consists of the following sub-headings: "Purpose and Organization" and secondly, "Introduction," which throw some light on the advantages of the effective, full participation of the "grass roots" toward effective economic planning.

The third part, "The Rationale of Economic Planning Decisions of Government Personnel," emphasizes the allocation of scarce resources in such a way that a sound foundation can be made on which prospective investment expenditures may lead to self-cumulative capital formation. The

allocation of these resources on alternative priority basis can be assigned within the context of long run growth model dependent upon the stage of economic growth.

The fourth part, "The Inadequacy of Market Prices for Plan Calculations," emphasizes full utilization of the factors of production through infusion of mobility and flexibility into these factors, which is not available in a market economy with its institutional rigidities inherent in the profit motivation system.

The fifth part, "The Planners and Economic Controls," stresses an optimal rate of combination of direct controls and indirect controls dependent on the stage of economic development for higher productivity.

The sixth part, "Employment and Unemployment," is concerned with the measures and steps toward realization of the full utilization of the factors of production, particularly labor. The capacity of the economy can be raised through different measures to attain an optimum rate of economic growth through full utilization of the factors of production, particularly labor.

The seventh part, "Administrative Structure for Implementation of the Second Five-Year Plan," implies that favorable administrative policies and measures precede the implementation of every successful plan. Decentralization

commensurate with ability and authority is the core of the problem of achieving higher productivity. This part also describes planning agencies, reforms in administration, public corporations, research, statistical data and allied problems, while the eight part summarizes the topics and points the way to certain conclusions.

### The Rationale of Economic Planning Decisions of Government Personnel

Allocation of Capital Investment Expenditures. "No less important for the planner are the problems of capital allocation. In fact, in view of the priority of capital, efficient allocation of resources, is usually given a central place in most plans."<sup>44</sup>

The allocation of scarce resources to economic projects whose contributions are quantitatively immeasurable such as education and health, or whose external economies cannot be correctly imputed, such as water and power, development, transport and communications, is requisite to the break through of economic and non-economic bottlenecks in the long run. Approximately 66 per cent of the real investment expenditures from the public sector and about 60 per cent of the total real investment expenditure from the first Five-Year Plan of Pakistan was spent on such projects as water and power development, transport and

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<sup>44</sup>

Muhbul El-Haq., op.cit., p. 32.

communication, housing and settlement, education and health. Planners had to decide the allocation of scarce resources to these so-called "economic and social overheads" whose benefits are so intangible and difficult to measure.

These sectors claimed about 60 per cent of total real investment expenditures in the revised Second Five-Year Plan of Pakistan. Aggregate investment expenditures in these sectors such as transport, power, irrigation projects housing, education, public health facilities, labor training centers, economic surveys and research create external economies. The cases of education and labor training centers can be cited for illustration. Investment in these sectors is responsible for higher productivity both within the projects and throughout the economy as a whole. The outlays on railroads, roads, and harbors will generate external economies by increasing their internal productivity. This internal higher productivity would help to lower the cost of their services to the rest of the economy in the long run. Some projects such as irrigation help only to set aside economic and non-economic bottlenecks making way for real investment expenditure. Their services provide essential inputs by which certain investment outlets become possible.

In the case of Pakistan, irrigation projects should not be considered as a part of the "economic and social overhead." It is merely an input in the agricultural sector and its economic advisability should be evaluated like any other input, such as fertilizer. In the first Five-Year Plan, the implicit capital-output ratio was 3.5 for major irrigation projects. Capital output ratio for intensive cultivation through improved fertilizers, seeds and farming techniques was 0.8. The planners must evaluate competing alternative allocations during these plans. The allocation of Rs. 1,710 million to irrigation, drainage, and colonization in the First Plan as against only Rs. 400 million to intensive cultivation, through good fertilizers, improved seeds, plant protection measures and better farming techniques (of which fertilizers claimed Rs. 200 Million) must have been evaluated. In the Second Plan, the allocation of Rs. 2,500 million to major irrigation work, as against an allocation of Rs. 400 million to fertilizers must have been weighed for economic feasibility. Irrigation projects have been stressed to construct an infra-structure of the economy.

Taking the view of a long-run growth model, short-run allocations should be curtailed in the area of social services. These include housing, health and social welfare services. Education, however, must be emphasized

although it is difficult to measure its exact link with economic growth model, except in the case of technical training. In the case of housing, health and social welfare services it is different. It is a fact that improvement in these sectors will help to enhance human productivity. However, allocation to more materialistic projects might help to raise the general productivity of the economy to a greater degree. Emphasis on these sectors might be considered as social rather than economic in nature.

Greater emphasis must be given those projects which yield external economies, e.g., more real investment expenditures for a labor-intensive technology, and labor training schemes which will help to bring forth higher external economies. This is particularly important for a country which lacks adequate capital goods and foreign exchange earnings, and is weak in creative adaptation of foreign technology. Emphasis on geological surveys, agricultural research for new varieties of crops, more productive means of production, industrial research for indigenous manufactured products, and mineral exploration would bring forth external economies, though less obvious and far-reaching in effect. Pakistan's revised Second Plan allocates Rs. 46 million to atomic energy, but only Rs. 8 million to research in fisheries. The latter is one of

the largest natural resources of East Pakistan and could earn substantial foreign exchange if properly emphasized. For higher industrial productivity, more allocations must be assigned rather than Rs. 20 million for technical training and apprenticeship in the industrial sector.

It needs also to be recognized that when different overhead facilities are believed to yield external economies, it is wise to concentrate expenditures in a few fields where visible results can be obtained quickly, and where there is a possibility of a snowballing effort. There is a tendency in underdeveloped countries, as pointed out by Hirschman and Galbraith, to spread their scarce resources too thinly over the entire system.<sup>45</sup>

With the spreading of scarce resources throughout the economy, the results obviously will be little improvement for everyone. Small stretches of roads are being built everywhere in the country, research centers are scattered all over, leading to duplication of efforts of staff and equipment, incomplete sewerage networks in all areas. The college of home economics, centers for the bling, low-cost housing for the poor, modern architecture for the old universities and construction of new universities in all areas, and so on, come in for a share of the allocations. Evidently, there is not sufficient

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<sup>45</sup>

Haq. op.cit., p. 37.



allocations for any one sector of the economy. Concerted efforts should be directed toward development of the inland water transport system of East Pakistan. This could help in accelerating the pace of economic growth of the entire region. The present policy of spreading allocations to cover roads, railways and inland water transport over the whole area must be changed; Pakistan's revised Second Plan allocates Rs. 420 million for roads and road transport but only Rs. 175 for inland water transport so far as East Pakistan is concerned. Similarly, an intensive utilization of fertilizers in a few selected areas of the agricultural would lead to higher productivity rather than efforts to provide all services inclusive of irrigation, agricultural extension, plant protection, and a host of other activities in all regions and areas through small and widely scattered schemes.

#### The Inadequacy of Market Prices for Plan Calculations

The case for using shadow prices in national planning has been well state by Tinbergen. The central point is that a number of market prices, particularly those of the factors of production (capital, labor, foreign exchange) often diverge from intrinsic value.<sup>46</sup>

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Ibid., p. 40.

The main objective of the planners is to derive a maximum rate of economic growth under a given amount of labor, capital and foreign exchange earnings within a specified plan period. They must emphasize the production of the maximum output--the full utilization of the factors of production. The prices prevailing in the free market economy are not designed to achieve this objective. The aim of the free market economy is to maximize private profits rather than the full utilization of the factors of production. Institutional rigidities and imperfection in the economic system prevent the market prices of the factors of production from approaching their equilibrium prices.

Reliable estimates indicate that both disguised and open unemployment presently prevalent in Pakistan is about 20 per cent of the labor force. (total working force). Capital can be borrowed at 6 to 8 per cent rate of interest in an organized capital market. On the other hand, in the unorganized capital market of the rural areas, borrowers are willing to pay 50 to 100 per cent rates of interest to money lenders. This reveals the existence of the scarcity of capital in the non-monetized sector of the economy. The average net yield (net profit rate) is approximately 30 per cent, in the large scale industrial sector,

while in some other sectors of the economy, the average net yield might be higher than this figure. The prevalent yield on long-term government bonds is about 4 per cent. During the middle of the nineteenth century<sup>47</sup> the yield on government bonds was from 7-8 per cent in the limited states especially when the scarcity of capital was not so acute, with reference to economic growth, as it is in Pakistan today. Interest rates on savings deposits have been ranging from 2 to 3 per cent, while on the other hand, wholesale prices have been rising to the extent of about 8 per cent per annum during the last five years. This indicates a negative yield to the savers. The rate of unemployment in East Pakistan at present stands at 33 per cent, while it is only 8 per cent in West Pakistan. The Prospect of labor mobility between the East and West wings is very dim. In Pakistan, the prevailing bank rate is 4 per cent. This interest rate is always influenced by the bank rate in the capital market. Net yield offered must be substantially higher for the attraction of sufficient net savings. An interest rate between 8-10 per cent would seem more desirable than the present rate of 4 per cent, for the mobilization of sufficient net savings in Pakistan.

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Source: "Census of Manufacturing Industries, 1959-60" Statistical Bulletin (Karachi: Central Statistical Office, November, 1961).

### The Planners and Economic Controls

"Economic controls are inherent in national planning, the aims of which is to change market preference in favor of a higher rate of growth than the free market would otherwise provide. But these controls can take several forms and it is the essence of pragmatic planning to find out, through experimentation, which particular set of controls suits a particular country.<sup>48</sup>

The allocation of scarce resources has been assigned particularly to the private sector, with the use of direct controls until 1960<sup>49</sup>. This committee has the authority to change the size of any particular investment expenditure. The assignment of key imports like steel and coal, are also subject to the decisions of this committee. Price and profit controls were clamped upon a number of commodities such as food grains, cloth, sugar and steel. Almost all private activities were subject to the veto of this committee.

The Civil Service of Pakistan was chiefly responsible for law and order in the country. Now it is confronted with the additional task of economic development. The

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Muhbul El-Haq., op.cit., p. 99.

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Since 1960 there has been a gradual relaxation of direct controls under a long-range decontrol policy of the Government of Pakistan.

Civil Service, however, had a profound suspicion and distrust concerning the operation of normal market mechanisms of the private sector. The institutional vested interests were also emphatic about this trend. Direct controls led to an enormous economic pawn in the hands of the officials responsible for government sanctions and the issuance of licenses. This became a source for supplementing the low salaries of some unscrupulous government officials. Direct controls are not generally effective, but they did help government employees, in particular, to obtain their supplies of consumers' goods at controlled prices. Strategic economic planning decisions could have done the same thing through the market price system instead of intervention to achieve a higher rate of productivity in the long run.

Haq describes one of the problems of direct controls as follows:

"Once direct controls were introduced, they bred like mushrooms. In order to control the final price of cotton cloth, the government started controlling the price of raw cotton, the dealer's margin, the manufacturer's costs, the distributor's profits, and a whole lot of related activities: and as the direct controls started replacing the market, the pyramid kept on building, till the government officials sitting on top of it did not know any longer what on earth they were controlling." 50

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Muhbul El-Haq, op.cit., p. 51.

Introduction of direct controls on economic activities became cumulative in the long run and this distorted the prospects of a free market economy, thus perverting the purpose for which the direct controls were imposed in the first place.

The introduction of direct controls in underdeveloped countries is not only dependent upon the institutional factor and vested interests but also upon the following: the required changes are of the nature of important structural changes rather than of the marginal character in the underdeveloped economies; quick, tangible results pertaining to the sufficient supply of the production of consumers' goods and the rate of economic growth are needed, but the operation of the market economy is believed to be slow, the non-monetized sector (which is not under the operation of the market price system) dominates the economies of these underdeveloped countries. Structural changes can be envisioned through price inducements provided they are sufficient. Adequate high interest rates can be a good source for the mobilization of savings. Suitable fiscal and tax changes (inducements) can help determine the size and pattern of private real investment expenditures. Relative changes in prices can help to allocate capital for an enhanced rate of economic growth.

Direct controls should be a supplement to these economic policies. A large, non-monetized sector can also be affected by indirect price incentives under the operation of the market price mechanism. The administrators should be able to utilize the higher productivity and efficiency of the market mechanism for the allocation of scarce resources.

An optimal combination of direct and indirect controls should be able to effect a desirable rate of economic growth and distribution within this system. The excise duty on tea was imposed with the intention of encouraging tea exports, but contrarily, a maximum export quota for tea was quickly set. Besides this, price controls were imposed on tea because domestic prices of tea had increased due to the higher excise duty. A bonus of earned foreign exchange in the form of retention of 20 per cent was given the exporters of cotton goods. Upon sizable export and resulting domestic shortage, a minimum quota was fixed for domestic consumption. According to national planning, the development of the agricultural sector was given top priority. For the protection of consumers, food-grain prices were controlled; consequently this adversely affected farm incentives for greater production. An export bonus scheme was initiated to encourage export of

manufactured goods. Paradoxically, most of these manufactured goods were consumed within the country because they were subjected to domestic price controls. The irony is that administrators have been trying to promote higher rates of economic growth and exports without any sacrifice in domestic consumption. On the other hand this implies that there must be a real sacrifice of domestic consumption, especially in the short run, for the ultimate attainment of the objective. There exists a widespread feeling among administrators that the operation of the price system (in the market free enterprise mechanism) is motivated by the accrual of maximum profits, and that the mechanism of the free market leads to the exploitation of consumers. But for equilibrium prices of foreign exchange, capital and other factors of production must be seriously considered in the allocation of scarce resources to competing priorities.

Price controls have resulted in cheap goods for a few of the fortunate in Pakistan; the rest of the economy has suffered either from shortages in the supply of goods or from black market prices. Controls on the allocation of foreign exchange availability did not help to keep prices down for the ultimate consumer. It only permitted a few vested interests (category holders of import licenses) to earn a windfall of economic rent (increased



increment). Low interest rates did not help provide a sufficient availability of capital for the small entrepreneurs. It only caused them to turn to the unorganized market with substantially higher rates. Low food-grain prices benefited only about 10 per cent of the population living in the urban areas, at a cost of 90 per cent to the agricultural population. The standard of living in the latter sector is dependent upon the prices of its marketable surplus. The pursuit of short run goals run counter to the long run objectives of self-sustained level of economic growth. Efforts through price controls do help to keep prices down, but often result in discouraging production and encouraging consumption. The gap between the actual supply of goods and the effective demand is widened. Lower interest rates and lower value of foreign exchange than their equilibrium prices serve to encourage the adoption of non-economic technologies. This in turn leads to wasteful use of scarce resources.

It should be possible for planners to fashion controls which would help to achieve self-sustained economic growth and social welfare with a higher rate of growth in productivity. The accrual of a socially desirable rate of economic growth would help to extend economic opportunities to the "have nots." If relief through special subsidies is needed in certain sectors of the economy, the

larger issue of economic controls should not be mixed with it. If relief is to be extended to the low paid government employees, direct additional taxation should be imposed to finance an increase in their salaries, rather than by controlling the prices of a number of commodities. If a particular industry is to be encouraged, a direct subsidy should be given rather than the provision of cheap foreign exchange. A lower price of foreign exchange only encourages the misallocation of resources, especially in the choice of technology, capital-intensive or labor-intensive.

The planners must weigh the opportunity cost of scarce government administrative personnel. Certainly, planners must avoid the common fallacy that the opportunity cost of scarce administrators is zero. Often good administrators are asked to administer a frustrating array of controls, involving the sanction of numerous permits and licenses, while the development projects in the public sector suffer delays and inefficiency from the lack of good administrators.<sup>51</sup>

The real investment expenditures in the public sector at present amount to about Rs. 3,500 million annually. Many examples can be cited where there have

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<sup>51</sup>Ibid., p. 53.

been undue delays and wasteful use of scarce resources in the public sector. This has resulted in hampering the economic growth of the private sector as well as the overall rate of economic growth. If there could be a shift of the present administrative personnel from control departments to economic development departments, a 10 per cent improvement in the rate of efficiency could be expected. Approximately, there would be an immediate gain of savings of Rs. 350 million and multiple effects on the rest of the economy could also be considered because of more efficient and speedy completion of government projects.

Although the declared policy of the government has been to assign highest priority to the agricultural sector, many of the controls run counter to this objective. The food-grain prices were held down through controls and this helped to subsidize the cost of living for industrial workers in the urban centers. The agricultural sector is responsible for earning a substantial foreign exchange but import licenses have been issued to the industrial sector. This indicates a windfall for the latter and an implicit transfer of income from the agricultural to the industrial sector. Also, the industrial sector has been given numerous tax concessions besides being assured a highly protected market for its inefficient products. Such policies implied

a concealed tax on the agricultural sector and a concealed subsidy for the industrial sector. The operation of these controls made agricultural investment an inferior alternative for the private sector.

Recently, Pakistan has been emphasizing the evolution of indirect, fiscal controls instead of direct administrative controls. The control on the price of food-grain has been lifted and support prices put into effect. The purpose of this policy is to effectuate food-grain prices within a specified range through the operation of buffer stocks. The control on prices and rationing in distribution have been done away with in most communities. Rigid import controls have been substituted for the most part by automatic renewal of import licenses upon their expiration.

Increased operational work in the field of economic and social overheads must be stressed by the planners. They must define more precisely infra-structure investments. The real investment expenditures in sectors that do not impart external economies, but are responsible only for the provision of certain imports must be de-emphasized. The allocation of scarce resources must be made especially on social services with special reference to proper perspective in the light of the growth philosophy towards a self-sustained level of economic growth. The planners must

emphasize those projects which yield genuine external economies and concentrate their efforts in fields where a breakthrough is possible in the economic and non-economic bottlenecks.

The planners must consider an optimum size of the aggregate real interest expenditures towards infra-structure sectors of the economy. This should be based upon desired demand analysis so that a marginal higher rate of productivity in the supply of goods might be used to finance a desirable rate of economic growth for the future.

The planners must carefully define the controls and policies which would help to implement their plans most efficiently. This is especially important during the early stage of economic growth. That administrative resources are scarce must be admitted. They do not have a zero opportunity cost, but rather a very high opportunity cost. Administrators should be concerned only with strategic decisions, leaving minute details of the allocation of scarce resources to the mechanism of the free market. Market preferences should be changed through indirect controls such as taxes and subsidies, rather than by direct administrative intervention in the market. This would tend to help raise the rate of economic productivity in the long run providing a self-sustained level of economic growth.

### Employment and Unemployment

Approximately six million people are presently unemployed in the country. Unemployment had risen during the last decade by about 2.5 million workers. According to the targets of the revised Plan, the additional labor force would be around 3.3 million workers, when the real investment expenditures of this plan would not create employment for more than 2.6 million workers.

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TABLE I

#### TOTAL LABOR FORCE AND ITS DISTRIBUTION (in millions)

Fiscal Plan	1 Total Labor Force	2 Agri- cul- ture	3 Indus- try	4 Serv- ices	5= 2+3 + 4 total employed	6= 1-5 Total un- employed
1950 (actual)	24.0	13.8	1.3	5.2	20.3	3.7
1955 (actual)	26.5	14.2	1.7	5.8	21.7	4.8
1960 (actual)	29.2	14.6	2.1	6.2	22.9	6.3
1965 (target)	32.5	16.0	2.6	6.9	25.5	7.0

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Planning, Mahbubul-Haq, The Strategy of Economic  
Table 10, p. 84

Emphasis should be placed on the expansion of the non-agricultural sector so that surplus labor from both the agricultural and the non-agricultural sectors will be gainfully employed. At the same time, there is some possibility of creating job opportunities if additional pieces of cultivable land can be brought under the plough.

In West Pakistan, twenty-one million acres of land were classified as cultivable waste in 1960. This land could be cultivated if irrigation, reclamation and drainage facilities were provided. Since this acreage is equal to 50 per cent of the land already under the plough, in West Pakistan, it appears that if only fifteen million acres of it can be brought under cultivation within the next twenty years at an average rate of three million acres per Plan period,<sup>53</sup> 2.5 million workers could be gainfully employed.<sup>54</sup>

Double-cropping would enhance the possibility of more job opportunities in East Pakistan. Out of a total cultivated acreage of 22.2 million acres, only 7 million are now being put under double crop cultivation in East

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One of the targets of Plan Two is provision of 2.2 mil. acres of new land through irrigation, reclamation and drainage facilities for 6.0 million in West Pakistan, P. 412.

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Mahhah Al-Haq, The Strategy of Economic Planning, Table 2-26, p. 244.

TABLE II

## POSSIBILITIES OF ADDITIONAL AGRICULTURAL EMPLOYMENT

(in millions of acres and millions of workers)

	<u>East Pakistan</u>				<u>West Pakistan</u>			
	1955	1960	1965	1970	1955	1960	1965	1970
Area now under cultivation	22.2	22.2	23.0	24.0	38.5	40.8	46.8	50.0
Area being double-cropped (mil.acres)	7.0	7.0	8.0	10.0	3.0	3.0	3.0	3.0
Total area available on single crop basis	29.0	29.0	31.0	34.0	41.5	43.8	49.8	53.0
Area required for one gainfully employed worker	4	4	4	4	6	6	6	6
Fully employed labor	7.3	7.3	7.7	8.5	6.9	7.3	8.3	8.9



Pakistan. A substantial increase in agricultural employment can be realized through the provision of new irrigation facilities in West Pakistan and through double-cropping in East Pakistan. The rate at which these employment opportunities will increase depends upon rational planning decisions by the planners. In the initial stages of economic development the agricultural sector may offer greater scope for new employment than the industrial sector.<sup>55</sup>

It seems clear than on the average an additional net capital expenditure between Rs. 4,000 and Rs. 5,000 is necessary if the additional employment opportunity is to be offered the workers. An increase in additional capital expenditure per worker may become a fact when large scale industry plays a dominant role in the economy. Average capital expenditure per worker in large scale industry amounted to about Rs. 7,000 in 1960.<sup>56</sup>

Greater emphasis upon the development of a capital goods sector in the future will lead to a rise in requirement of capital expenditure per additional worker. The

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It should be noted that the nature of "new" employment opportunities in the agricultural sector is not the same as in the industrial sector. Previously unemployed may become employed by these new methods.

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Taken from Census of Manufacturing Industries, 1959-60, total capital reported to be Rs. 3,193 million total employment 450 thousand.

utilization of labor intensive technology, especially for the development of consumer goods, especially of small scale enterprise, would help to provide more opportunities to the workers at less cost. Construction projects such as roads, housing and irrigation can help to absorb the labor gainfully.

### Administrative Structure for Implementation of the Second Five-Year Plan

Favorable administrative policies and measures precede the implementation of every successful plan. To a great extent the Community Councils are responsible for the execution of different plans and programs directed to the economic development of the rural and agricultural sectors.<sup>57</sup> Private entrepreneurs are chiefly responsible for industrial development. More emphasis is being placed on the initiative and judgment of private enterprise in bringing about the desired development of the industrial and commercial sectors. As far as public policy is concerned, important administrative reforms were initiated during 1958-60<sup>58</sup> for decentralization in the implementation of various development programs. The responsibility and discipline of the public sector is being stressed by

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<sup>57</sup> Under the "basic democracies" the Community Councils are vested with these powers. Page 105, Revised Second Five-Year Plan.

<sup>58</sup> Ibid., p. 106.

the elected representatives of the local councils. The administrative agencies of the government must be able to perform the concrete task of programming and execution of the plans in the long run.

Planning Agencies. In June 1959, the Economic Council was organized as the supreme decision-making body for economic policy and progress.<sup>59</sup> The Council was headed by the President and consisted of the governors of the provinces, the ministers of the principal development ministries, the chairman of the P.I.D.C. (Pakistan Industrial Development Corporation), East and West Pakistan W.A.P.A. (water and power development authority) and the chairman of the Planning Commission. Its functions are as follows: (1) to formulate economic policies according to the overall economic position of the country; (2) to scrutinize the Five-Year plans; (3) to sanction development schemes including those falling under the Five-Year plans and the annual development programs, and (4) to appraise the progress of economic development due to these plans and programs.

There is also an economic committee of the Cabinet below the level of the Economic Council, which performs the following functions: (1) the supervision of the

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Ibid.

implementation of the economic policies of the Cabinet and the Economic Council, (2) making of decisions on day-to-day economic problems, and (3) giving sanction to development schemes pending their submission to the Economic Council. The Economic Committee is headed by the Minister of Finance and consists of other members and the Chairman of the Planning Commission.

The Planning Commission has been given a new charter with such authority and responsibility as is appropriate for a central planning agency. Its functions are: (1) the preparation of a national plan subject to periodic assessments of the human and material resources of the country, (2) determination of priorities and proposal for the allocation of resources, (3) coordination and examination of development programs and projects of different government agencies, (4) an evaluation and appraisal of productive efficiency in the implementation of the development program, (5) initiation and promotion of economic research, surveys and investigations to support effective planning and development.

The supervision of the implementation is turned over to a new agency which is known as the Projects Division. Its duties are as follows: (1) to promote the progress of the implementation of approved development projects, particularly aided projects, (2) distribution of progress

reports pertaining to various development projects, (3) initiate creation of institutions of basic democracy. Development responsibilities are being shared by elected representatives and appointed officials. The Councils operate at union, tehsil, thama, district and division levels. The institution of Basic Democracies can be expected to assume an important role in a decentralized economic development planning and implementation for economic growth.

"The Basic machinery is thus seen to be established to do an effective job of planning and implementation. However, this machinery will require refinements and adjustments to achieve the high standards of administrative performance needed for the Second Plan. Certain questions of crucial importance will require early resolution; others cannot be resolved without additional experience, and will then require extensive study and improvement, perhaps throughout the Plan period."<sup>60</sup>

The role of the Economic Committee of the Cabinet is very important in the solution of current problems through the making of sound decisions. For the effective implementation of different projects and programs, a more decentralized authority in favor of the provincial governments is required. The principal planning and development

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The Second Five-Year Plan, op.cit., p. 109.

departments should play an increasingly effective role in initiating and coordinating planning within the provincial governments. The heads of the planning and development departments should be able to demarcate an optimum balance between the planning and the execution of development programs. Efforts towards efficiency both by the Planning Commission and the provincial planning departments have resulted in the improvement of the quality of planning through the government machinery.

Reforms in Administration. The optimum decentralized organization, especially in the number of layers of administration, is a very important requisite for efficient allocation of responsibilities and trained personnel. This would help coordinate different programs and development projects more effectively. The institution of Basic Democracies would impart much flexibility toward the emergence of a democratic pattern of administration. This would lead to a maximum degree of self-government not only at the local level but also to a degree of public representation in administration at successive levels. These will be more meaningful if only in a measure of local planning and policy formulation were given serious consideration at the level where final government decisions are taken. Probably the best opportunity exists for democratic participation in the area of development planning.

In sum:

"The First Plan dealt at some length with certain characteristics of central and provincial administration which were considered to be ill-adapted to contemporary needs. Strong recommendations were made for modifications of the administrative system towards clear-cut organization, and broad delegations of authority, with staff officers removed from the line of command. Many checks and balances and time consuming discussions at lower levels were to be eliminated."<sup>61</sup>

During 1959,<sup>62</sup> reorganization bodies were set up to overhaul the central and provincial administrative machinery.<sup>63</sup> There must be an optimum balance between policy framing and executive function so that over-centralization of authority does not hamper effective field operations. Long-range programs should be broken down into annual development budgets so that they will become an integral part of the financial management.

Improvement of coordination between development programming and budgeting would also be extremely desirable. In 1959-60, the system of budgeting and financial controls was reformed upon the recommendation of the control administrative reorganization committee. The importance of budgeting was recognized as an instrument in the administration of development. Budgeting should become a continuous process and the preparation of the budget should

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<sup>61</sup> Second Five-Year-Plan, op.cit., p. 112.

<sup>62</sup> Revised Second Five-Year Plan, p. 112.

<sup>63</sup> Ibid., p. 113.

be made twelve months ahead of the financial year. As long as there is no commitment of budget appropriations, the system of expenditure authorizations should be abolished. An important reform was introduced through coordination and integration strengthening the system of development working parts. This implied the coordinated efforts of the administrative bodies for the scrutiny of development schemes and programs. Efforts should be made toward further integration of the planning and budgetary processes so that the annual development programs may be clearly identified both in the budget and in the Five-Year as a whole.

New reorientation must be imported to the civil service of Pakistan. The responsibility toward the expeditious implementation of economic development programs must be given consideration. Closer and more effective association of both administrators and technicians can only accelerate the rate of productivity when an optimum organization with decentralization can be emphasized in the economic system. Particular emphasis on the demarcation of well-defined responsibilities in such optimum organization will eliminate inefficiency and red-tapism. Excessive responsibilities and over-centralization will prove a retarding factor toward the desired objective of self-sustained level of economic growth within the foreseeable future.



In the words of the Second Plan:

"The problem of filling the personnel needs of the public service is not so much of interesting the most talented in government employment (although, the competing attraction of more remunerative business careers is making this increasingly uncertain) as of making up somehow for the shortage of skilled personnel through training and economical use of available talent. Trained personnel is a very scarce resource, and is likely to continue so for some time to come. The most careful attention to personnel selection, training and use is therefore imperative and is certain to pay large dividends."<sup>64</sup>

The supply of the scarce resource of trained personnel could be made more elastic if proper efforts were put forth. Personnel selection, training and their usage have been handled effectively through the establishment of Division Centers for higher productivity in their performance. The task of personnel management should undergo a change for the betterment of procedures so that the complexity produced by the growing size of the government machine can be successfully grappled with. The introduction of new concepts of administration in the Basic Democracies along with the initiation of well-planned training programs would help materially in the infusion of democratic ideas in administration in Pakistan.

The various training programs for the attainment of this objective are as follows: The Civil Service of

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<sup>64</sup>

Second Five-Year Plan, op. cit. p. 116.

Pakistan Academy <sup>65</sup> and the Finance Officers Academy provide highly specialized technical training for entry into these superior services. They are fully equipped with curricula designed to focus special attention on the problems of administration pertaining the administration of development programs. The academies for village development help to provide a specialized post-entry training for officials. These officials are thoroughly familiar with the problems and techniques of development administration. An administrative staff college has been established to raise the efficiency of senior officers (civil service officers particularly) through more research, organized consultation, and formal courses for senior officers.<sup>66</sup> The Institute of Business and Public Administration at the University of Karachi provides graduate training courses. It is felt that the Central Personnel Agency should institute a continuous review of the effectiveness of these institutions. The determination of the need for new training institutions for the public services should be an important function of this agency.

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<sup>65</sup>  
Ibid., p. 117.

<sup>66</sup>  
Ibid.

Public Corporation. By 1955, several public corporations such as P.I.D.C. (Pakistan Industrial Development Corporation) had been established in the interests of providing greater flexibility towards the management of government operations.<sup>67</sup> The West Pakistan W.A.P.D.A. (Water and Power Authority) was founded and the East Pakistan W.A.P.D.A. was created in 1959. The inland water transport authority was in East Pakistan in 1958, vested with board authority. A Forest Industries Development Corporation was set up in East Pakistan in 1959 also. In West Pakistan, the Road Transport Board was formed in 1957. A corporate form of administration was introduced covering small and cottage industry development; the Small Industries Corporation was created in 1955, at the Center, while the Small Scale Industries Corporation of East and West Pakistan respectively were established in 1957 and 1960.

The general problems handled by these public corporations are as follows: (1) effective policy control by the government; (2) the proper coordination between agencies and departments involved in development activities. The authorities and corporations should be coordinated in such

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<sup>67</sup>  
Ibid., p. 118.

a way as to insure maximum possible administrative flexibility. Administrative flexibility can only be infused when, through decentralization, their internal management is left essentially in their own hands. Their productive efficiency can be enhanced through economies in expenditures and wise management of finances.

#### Research, Statistical Data, and Allied Problems.

The rate of economic development is greatly dependent upon the rate of increase in the vitality of technical research. Emphasis upon more effective organization and support of basic and applied research in physical, biological, and social services will lead to a higher rate of productivity in the long run. Modern methods of research are both qualitative and quantitative in nature and are subject to application both in the laboratory and in the field. These require advance planning of personal and facilities, coupled with the analysis of mass data which can be primarily derived from the statistical services of the government.

The Central Government has set up various independent or quasi-independent research agencies in recognition of the limitations of research efforts within operational departments. These operational departments include the Geological Survey of Pakistan (1947), the Cotton

Committee (1948), the Food and Agricultural Council (1949), the Inter Committee (1950), Pakistan Medical Research Council (1953) and the Atomic Energy Commission (1955). The Cotton Committee supports itself through a levy on production, but the other bodies are mostly financed by the government. Lack of organization has retarded the progress of technological research. Development of an independent and efficient national system of statistics should be encouraged outside government jurisdiction. In the private sector there is a dearth of adequate scientific and industrial research designed to raise the productive capacity and also to improve the quality of the products. Facilities for scientific and industrial research should not only be encouraged but also extended for the attainment of the cherished goal of adequate capital formation.

Research is mostly intended to assist in the determination of administrative policies and evaluation of programs, projects, and the planning processes within the government sector. On the other hand, research in the several disciplines of the social sciences is being conducted in the universities and under the guidance of a few independent research agencies outside of the government sphere. Research on income distribution is most important in predicting the allocation of scarce resources for economic development in the future. This could be utilized

to help guide future policies for reducing extreme inequalities. Research studies are needed to improve the basic data for national income estimation, for the pattern of consumption at different income levels is extremely important as it pertains to the basis of the forecast of demand schedules. The planning production programs and measurement of the effects of development on welfare can also be deduced through the availability of these basic data. Provision for the establishment of a council for research in social sciences was made in the first Five Year Plan. This council should be able to develop a broad research program in social sciences, thereby assisting the government in the application of the findings for the solution of problems of economic development. Sufficient development of broad programs of essential economic research will be possible only through the cooperative efforts of the Council and other research agencies in the country.

The establishment of special libraries should be supplemented by the pooling of reference materials through inter-library loans, lists and catalogs, and cooperative bibliographical work. It is very heartening to realize that international reference services are available to a great extent to assist in the training of special librarians. With the development of special libraries, the establishment of a central catalog will be necessary.

The establishment of the national sample survey, in 1956, was to supplement the Central Statistical Office (C.S.O.). The West Pakistan Statistical Bureau was set up in 1957 and since that time has undertaken certain important surveys. It has also developed its internal operation; statistical coverage has not been sufficient, the principal deficiencies being found in the estimates of population, in the figures for agricultural output, statistics of manufacturing industries and published data pertaining to trade. Regular statistics for fisheries and forestry and livestock are not yet available. The collection of current statistics regarding labor and unemployment is still confined to Karachi, and only limited information pertaining to the occupational composition of labor is available. Statistics relative to wholesale and retail trade are not yet supplied in any great amount. Estimates of gross capital formation and national income at current prices are also lacking. The general index of prices should be improved and the improvement of basic price data should be encouraged.

The aggregate figures of development expenditures compiled by the various departments do not always tally because of the divergence in definition, methods of compilation and sources of information. Irrelevant

classification of some commodity imports such as defense goods leads to the distortion of commodity totals. Imprecise and ambiguous classification in budget accounting, and the maintenance of large expense accounts over long periods creates difficulties in making economic analyses. The better interpretation of data can be facilitated by the development of seasonal corrections for fluctuating prices. The value of statistical data can be enhanced if they are published without delay.

It is imperative that all ministers and departments which are concerned with development responsibilities have statistical units (as a part of the planning cells). To further the development of comprehensive and integrated programs, the Central Statistical Office should act as the national statistical authority. It should serve as the coordinator among the agencies in this particular area, in the collection, maintenance and analysis of statistical information. Planning and coordination by the Central Statistical Office should be subject to evaluation of need, the development of uniform statistical standards, uniform definitions and classification systems, clearance and scrutiny of survey plans, and the allocation of agency responsibilities.

The Central Statistical Office should intensify its activities in fulfilling its primary function. It should



provide technical advice to the central ministries regarding the collection, maintenance and analysis of statistical information. This would insure the standardization of information collected thus providing fuller utilization of data collected by various statistical units. It should also provide mechanized facilities in the Central Statistical office to various ministries and departments for the tabulation of such data. It should not only coordinate the work relating to planning, production and publication of statistical information, but also provide training facilities in statistics.

Training is needed both in the techniques of statistical operations, and in statistical methods. Statistical operations have become large scale undertakings to a great extent and they require a high degree of management. The long run growth model recognizes the permanent importance of research specialists and statisticians. The services of scientists, economists and statisticians should be established on a permanent basis. The requirements for research and statistical development must be fulfilled through the utilization of the services of the highest levels of professional talent. A standing advisory council consisting of the principal statistical agencies of the government, and the principal area of statistics should be appointed to keep under constant review the organization, efficiency, and adequacy of the statistical services

and the establishment of statistical standards.

### Summary and Conclusions

1. New ideas, inventions, and technology for a higher level of productivity can only be visualized when effective "grass roots" participation is achieved. Decentralization commensurate with authority and ability for the full coordination and unification for a common goal is a prerequisite for a higher level of national income.
2. Concentration of the allocation of scarce resources would help toward a breakthrough of both economic and non-economic bottlenecks. Capital overhead investment expenditures might be preferred to social welfare programs in the interest of a self-cumulative rate of capital formation for a long run growth model, especially in the initial stages of economic development.
3. Full utilization of the factors of production is not possible under a free market economy, whose motivation is higher profits. Institutional rigidities and vested interests form a factor leading to underutilization of these factors. The net savings for higher real investment expenditures can be raised if a more attractive rate of interest is

offered as compared to the prevalent net yield for lenders.

4. An optimum combination of direct and indirect controls must be stressed for realization of a higher rate of productivity. This combination should be used in such a way that incentive to work, produce, save, and to take risks for new technology and inventions, can be enhanced to an optimum level. Emphasis on real investment expenditures must be stressed at the cost of production of consumers' goods especially for the short run. The allocation of scarce resources of administrative personnel can be utilized in the interest of implementing development programs rather than in the introduction of direct controls.

5. Through the provision of additional acres of cultivable land, labor can be more fully utilized, while irrigation and double-cropping in both East and West Pakistan can raise the level of productivity in this sector of the economy. Labor-intensive technology might be stressed, especially in the area of construction of both social and economic capital overhead. Emphasis should be placed upon measures designed to help create a sufficient cumulative rate of capital formation, so that

through the mobility and flexibility of the factors of production an increasing supply of labor can be fully utilized. The capacity of the economy to absorb an increasing population labor force can be implemented only if the rate of capital formation is made sufficiently elastic to be proportional to the rate of growth in population.

6. Efforts are being made to secure the effective participation of the "grass roots" for a continuous rate of economic growth and a higher stable rate of productivity. Through introduction of "Basic Democracy," elected representatives, and through specialized economic councils, planning agencies, decentralization corresponding with respective ability and authority are being emphasized.

The consistency and efficiency with which the allocation of scarce resources toward alternative priorities are being administered is also coming under scrutiny on a rational basis. Several public corporations have been established in the interest of coordination and implementation of various development programs. Research institutions have also been created for the adoption of economic models which would lead to a self-cumulative

rate of capital formation. Statistical bureaus have come into existence for the compilation of both macro and micro economic analysis. It will, however, take some time before the optimum participation of the "grass roots" can be secured in bringing about effective planning agencies, and for the availability of adequate statistical data pertaining to micro and macro components of the economy to be instrumental in the implementation of models leading to a self-sustained rate of economic growth.

## CHAPTER VII

### SUMMARY AND CONCLUSIONS

#### Summary

Summary of Chapter I. Chapter I is an introductory statement of the purpose, scope, and organization of the dissertation. The theories of programming and maximum social benefit have been emphasized throughout. These two theories form the basis of evaluation so as to arrive at the level of self-sustained economic growth under a given pattern of allocation of alternative priorities. Under a national program, private entities will have to be adjusted to the plans of the government sector. An optimal combination of the government and private sectors should be achieved to produce a desired rate of economic productivity. The long-run model, according to these theories, emphasizes the rate of increase in productivity brought about by an optimal rate of net savings, high enough to overcome the rate of increase in population thus producing a higher per capita income. The purpose of economic planning is to coordinate and allocate scarce resources in such a way that a self-cumulative level of economic growth can be attained within the shortest possible time. Evaluation

relative to alternative priorities for the attainment of this objective is extremely important. The requisite economic basis is also very important if the rate of economic productivity is to be raised accordingly.

The organization of the dissertation is given in this chapter in order to make the dissertation more meaningful, well-organized and well-systematized, and thus of greater benefit to the reader.

Summary of Chapter II. The second chapter describes planning in different types of economic systems. It emphasizes the importance of the mobility and flexibility of the factors of production under the theory of programming and maximum social benefit. Overcentralization and rigidity under communist types of economy and lack of effective planned coordination in the so-called "mixed economies" lead to a lower rate of growth in productivity in the long run. Decentralization and the optimum utilization of the factors of production would be extremely important requisites for the achievement of a continuous rate of productivity higher than the rate of increase in the population.

Planning emphasizes the coordination, direction and allocation of scarce resources in such a manner that a socially desirable rate of economic growth can be realized

and maintained for both social and economic stability. The role of the government in the underdeveloped economies should be to focus its attention upon essential aspects through imparting decentralization and elasticity of the factors of production. The main objective of the attainment of a continuous rate of economic productivity should be faithfully adhered to. The government's role must be to equip economic planning in such a way that economic and non-economic bottlenecks can be set aside. The role of the government sector in the underdeveloped economies is a very significant one in achieving the optimum combination of the government and private sectors. It must cement the foundation of the economy so that a long range growth model can be attained. The allocation of scarce resources must be made among alternative priorities so that an optimum rate of productivity will be obtained in the long run.

In any form of government planning, net savings or capital formation is the pivotal point around which the availability of scarce resources for allocation revolves. In a communistic form of government, centralized control of these net savings is demarcated between consumption expenditures and investment expenditures, with greater emphasis being placed upon investment expenditures. Decentralization would help to create greater flexibility



for the application of the theory of programming. In the modern democratic (developed) countries both the government and the private sector are responsible for these net savings. Mixed economies with rigidities help to create inflationary spirals even before full employment of the factors of production are realized. Under national planning the coordination of these net savings channels them in such a way that flexibility, instead of rigidity is the result; full employment of the factors of production is maintained at a non-inflationary point.

In the underdeveloped economies, the optimum net savings can be acquired through internal saving, loans and assistance from foreign countries, and through deficit financing. If the metallic base is strengthened by the government sector at the initial stages, both the private and the government sectors could achieve a desirable rate of capital formation in the long run. An optimum rate of combination between these two sectors could be demarcated only if economic and non-economic bottlenecks can be eliminated under a long run economic model.

Summary of Chapter III. In this chapter, initial views and analyses have been discussed. In order to raise the per capita income, net savings or capital formation must be at least two to four times higher than the rate of increase in population. If the rate of increase in the

population can be lowered, the requirements for net savings for raising economic productivity can also be reduced, probably within two to four times, depending upon the decrease in the rate of population growth. An optimum rate of increase which would be socially desirable in raising economic productivity must be substantial enough to maintain long run economic and social stability.

The economic plans must be within the consistency and efficiency of the given scarce resources if a given objective is to be realistically achieved.

The rate of economic productivity could have been higher had an efficient allocation of scarce resources been directed toward strengthening the metallic base of the economy. Wheat surplus under PL 480 could have been substituted for the domestic production for cash crops. A higher level of cash crops could have been an important factor in the earning of more foreign exchange, statistical data pertaining to both micro and macro economics are not available, and without these, the application of theories of programming and maximum social benefit are difficult to establish. Decentralized administrative organizational leadership could have helped in a great degree to enhance and accelerate the implementation of the real resources of the economy. The governmental sector

could have been more effective in eliminating social, economic, and non-economic bottlenecks through greater real investment expenditures favoring social overhead capital investment expenditures.

Summary of Chapter IV. The total amount of local currency in the original plan stood at 1,208 (crore rupees), while the aggregate amount of foreign currency in the original plan amounted to Rs.935 (crore). The total amount of local currency in the revised plan amounted to Rs. 1,471 (crore), but, on the other hand, aggregate amount of foreign currency in this latter plan was Rs. 1,319 (crore). The combined aggregate amount of local and foreign currency in the original plan stood at Rs. 2,143 (crore), but, the sum of both local and foreign currency in the revised version amounted to Rs. 2,790 (crore).

There were four sources of funds through which the plan was financed: savings, taxation, foreign aid, and deficit financing. Total savings for the entire original plan formed 35 per cent, but there was a decrease to 27 per cent, according to the revised version. The accruals from taxation in the original plan consisted of 12 per cent but these accruals rose to 14 per cent in the revised version.

The total supply of foreign exchange through foreign aid and foreign assistance for the overall original and revised Second Five-Year Plan, inclusive of both the Indus Basin replacement works and the works program, amounted to 49 per cent and 59 per cent respectively. Deficit financing was not undertaken for the revised version but, according to the original plan, it formed 4 per cent of the total accruals.

Convertibility, or multilateralism, has been the cherished goal for both purchases and sales in the international market. Diversification of both foreign and internal trade is dependent upon the productivity of the agricultural sector in order to accommodate the desired demand of the highly industrialized countries. Mobility and flexibility of the factors of production are based primarily upon an optimum level of the rate of productivity attained in the agricultural sector. The gap in the capacity of response of these factors will widen to an extent where the derived demand in the international market cannot be fully accommodated. Efforts should be made to keep the pace at which industrialization is being accelerated and also the capacity to cater to the desired demand by so-called underdeveloped economies.

Summary of Chapter V. More elastic monetary and fiscal measures are not only needed for economic stability, but also for a desirable rate of growth in net savings. Emphasis has been made upon taking a considerable part of the economic rent from both the agricultural and industrial sectors. This would help not only to lower consumption expenditures on luxury goods but also to accelerate the accumulation of real net savings toward raising the rate of economic productivity in the economy. Through the application of flexible monetary and fiscal operations, productivity has been kept at a higher level than the rate of increase in population growth. The supply of elastic credit through the commercial banks and specialized credit institutions to the various micro and macro segments of the economy is an extremely important prerequisite for the utilization of the full capacity of the economy. Implementation of indirect controls, through the operation of monetary and fiscal measures, tend to be more effective and productive as compared to direct controls in the long run.

In the developing economies, the threat of an inflationary spiral is always imminent; this is particularly true in the short run. The outlays of real

investment expenditures generates more income as compared to the supply of goods and services available. Long term maturities with higher rates of interest can be floated for the continuous stability of the rate of economic growth. Judicious spacing and timing of these long term maturities can be handled so as to accelerate capital formation without inflationary spirals resulting in the misdirection and misallocation of these scarce resources.

Summary of Chapter VI. The first part of chapter six emphasizes the long run self-sustained level of economic growth within the foreseeable future via the effective participation of the "grass roots" element. This would help to accelerate a continuous rate of economic growth leading to attainment of a socially desirable rate of net savings to counterbalance the increasing rate of population growth. Decentralization with respect to authority commensurate with ability would also prove extremely productive.

Allocation of scarce resources among relative alternative priorities should be made with special reference to the stage of economic development. A metallic base must be cemented in the so-called underdeveloped economies in the initial stages in the interests of demonstrating a cumulative rate of capital formation. Social welfare programs and other measures relating to

the fair distribution of income could be delayed until a later stage of economic growth where the rate of productivity has begun to rise at a faster rate compared with the rate of increase in population growth.

Labor-intensive technologies can be preferred to capital intensive projects in the beginning; these latter could come in a later stage along with a higher economic development. Government personnel should concentrate their efforts toward the timely implementation of these plans rather than concern themselves with the manipulation of direct controls. Indirect controls through fiscal and monetary measures would help to attain the desired objectives more effectively as compared to their application through the usage of direct controls. The marginal utility from the allocation of scarce reserves from every sector can be maximized only if the government personnel could be urged to enforce implementation of these scarce resources rather than the enforcement of direct controls.

The problems of inter-sectoral, intra-sectoral and infra-structural rigidities should be considered in the light of elimination of rigidities in the long run. Priorities for alternative allocations of scarce resources can also stress such projects as irrigation schemes, construction, highways, and so on. Allocation for alternative

priorities (inter-sectoral, intra-sectoral and infra-structural) are highly dependent upon the rate of agricultural productivity effectuated within the context of long-range growth model. Statistical data pertaining to micro and macro aggregative economies are extremely important when considering the feasibility of alternative priorities allocations for maximum social benefit--these data are rarely available in the underdeveloped countries.

### Conclusions

A Long-Run Growth Model. The theory of programming, as advocated by Professor Jan Tinbergen, through the application of social maximum benefit has been the main foundation of this dissertation. It has been subjected to criticism on realistic and practical bases.

Both flexibility and mobility of the factors of production (land, labor, capital and enterprise) are subject to limitations and institutional rigidities, even in modern highly industrialized nations. The presentation of this model tends to infuse a dynamism which is extremely important for the creation of harmony and coherence in the systems. An optimum expenditure of human potentials may never be derived because of natural human egoism and self-centeredness. Under the given theory of programming, national planning might tend to over-centralize the



government sector at the cost of dynamic rate of economic productivity because of private enterprise. This model is an eye-opener for those who fail to utilize the full capacity of the economy at the cost of substantial loss of real increment of economic productivity.

The price system, important for equilibrium between the given demand and supply of goods and services (both in the short and the long run), is not always consistent with the dictates of rational developmental planning. At the same time, a long growth model stresses the importance of indirect controls through monetary and fiscal operation rather than detailed direct controls.

A long run growth model emphasizes the importance of an adequate function of consumption expenditure. The fulfillment of present needs for a supply of goods and services is extremely important to assure a smooth and continuous rate of economic productivity. An optimum combination of government and private sectors is also a variable factor dependent upon the stage of economic development of a particular economy. In reality it would be difficult to demarcate the exact limits of the rate of combination which features government and private sectors because the government sector would always tend to dominate the decisions for demarcation.

An optimum level is not an exactitude but a variable which can never be reached. Psychologically, it stimulates operation of concerted efforts toward this cherished objective. This model implies and assumes the existence of political stability under which the operation of alternative priorities is carried out. Historically, this phase of economy has never been prolonged for a long period of time. Human egoism and selfishness have been responsible for the disruption of stable economy. In the underdeveloped economies, two-way communication may never be achieved due to superstition and ignorance of the majority of the citizenry.

It must be remembered that it takes a long time to build up a sound economic and non-economic atmosphere for an optimum level of productivity. Nationalism might be used to muster coherence and secure adherence to national programs which are extremely beneficial in the attainment of a desirable rate of economic growth. The tools of capital-output ratios do help in the realization of alternative priorities for optimum results. In conclusion, it can be said that this model offers challenges and dynamism which can be desirable at a critical stage replete with confusion and devastation. It brings forth a dynamism based on the realization of this model for

those who are interested in the economic development of underdeveloped economies particularly.

### Achievements and Problems

Most of the physical targets of production were attained during the Second Five-Year Plan of Pakistan. Gross national product, and its various components, has increased significantly, as shown in Table . Also, growth has been accomplished with minimum reliance upon direct controls and without large scale inflation. In addition, under a program of basic democracy, decentralization has been initiated. Efforts have been made to infuse greater rationality into economic planning through the establishment of various agencies. A foundation has been laid for the effective participation of "grass roots," even though it will take a long time for the exploitation of human resources to reach an optimum level.

At the same time, there have been problems. The allocation of scarce resources could have been intensified towards the installation of the steel industry so that new technology and innovations could have resulted in self-sustained long-run growth. A large increase in the supply of steel, not only for the agricultural sector, but also for small-scale and heavy industry, could have

TABLE I

## GROSS NATIONAL PRODUCT OF PAKISTAN AT CURRENT FACTOR COST \*

(1959/60 to 1964/65) <sup>68</sup>

	(Million Rupees)					
	1959/60	1960/61	1961/62	1962/63	1963/64	1964/65 <sup>70</sup>
1. Agriculture	16,753	18,465	18,879	19,752	20,075	21,919
(a) Major Crops	(9,634)	(10,853)	(10,835)	(11,501)	(11,378)	(12,507)
(b) Minor Crops	(2,180)	(2,299)	(2,476)	(2,515)	(2,668)	(2,913)
(c) Livestock	(3,719)	(3,979)	(4,054)	(4,165)	(4,248)	(4,322)
(d) Fishing	(1,111)	(1,212)	(1,368)	(1,306)	(1,588)	(1,970)
(e) Forestry	(109)	(109)	(146)	(175)	(193)	(207)
2. Mining and Quarrying	70	84	91	105	124	150
3. Manufacturing	2,930	3,316	3,713	4,165	4,603	5,042
(a) Large scale <sup>69</sup>	(1,565)	(1,883)	(2,236)	(2,621)	(3,006)	(3,381)
(b) Small scale	(1,365)	(1,433)	(1,477)	(1,544)	(1,597)	(1,661)
4. Construction	651	804	1,009	1,136	1,774	2,057
5. Elect.gas., water and sanitary services	107	124	133	182	258	328
6. Transportation, storage and communications	1,857	2,094	2,158	2,335	2,568	2,809
7. Wholesale and Retail Trade	3,665	4,179	4,440	4,679	5,109	5,654

TABLE I Continued

	1959/60	1960/61	1961/62	1962/63	1963/64	1964/65	70
8. Banking and Insurance	224	280	289	317	360	414	
9. Ownership of Dwellings	1,772	1,831	1,941	2,024	2,180	2,337	
10. Public Administration and Defence	1,331	1,430	1,493	1,560	1,859	2,137	
11. Services	2,112	2,231	2,376	2,465	2,720	2,948	
12. Gross Domestic Product	31,472	34,818	36,522	38,720	41,630	45,795	
13. Net factor income from rest of world	---33	---32	---37	---78	--115	--115	
14. Gross National Product	31,439	34,786	36,485	38,642	41,515	45,680	
Population (Million)	98.88	101.45	104.09	106.79	109.56	112.41	
Per Capita Income (Rupees)	318	343	351	362	379	406	

68

Time reference of the estimate is July-June.

69

Estimates of large-scale manufacturing have been computed on the basis of the New Index of Industrial Production and are not comparable with the previous series.

70

with Provincial

\* Government of Pakistan, President's Secretariat, Planning Commission, Evaluation of the Second Five-Year Plan (1960-65), May, 1966.

led to higher output and to more mobile and flexible factors of production. Real savings could have been sufficient to counterbalance the rate of increase in per capita income. The present allocation of scarce resources were not concentrated so as to set aside both economic and non-economic bottlenecks for a higher rate of economic growth and productivity.

The metallic base of the economy could have been strengthened so as to utilize the factors of production to full capacity, especially the labor factor. With the infusion of greater flexibility and mobility of the factors of production, the pace of industrialization could have been accelerated so as to pay for imports of both development goods and non-development goods for the full utilization of capacity of the economy.

Emphasis has been given to the establishment of some agencies pertaining to micro and macro aggregative economic statistical data. But more substantial research and statistical institutions are required so that maximum social benefit and linear programming theories can be effectively applied. Accurate alternative priorities can only be available when sufficient economic data can be attained through weighing social marginal cost and social marginal benefit from all angles with the transformation

of non-monetized sectors to monetized ones.

The consumption function has not been given sufficient consideration when capacity to produce for consumers' goods is limited particularly in the short run. Long run maturities with attractive yield have not been visualized so that higher income generated through real investment expenditure can be mobilized in such a way that a desirable rate of productivity can be found without threat of an inflationary spiral.

A competitive system would help to break through the economic and non-economic bottlenecks and with flexibility and mobility of the factors of production so that the required imports could be paid for through sufficient exports, thus keeping labor not only fully employed with optimum productivity but also full capacity of the economy, can always be fully utilized, thus making it possible to reach a self-cumulative rate of capital formation.

An optimum combination of the government and private sectors need to be demarcated, dependent upon the stage of economic development so that an economic foundation can be laid. With private enterprise, new technology, innovations, and higher productivity under profit motivation can be initiated. Direct controls, although few, by the governmental sector, have probably thwarted the adequate initiative of private enterprise during the Second

## Plan.

Economic rents from all factors of production can be more fully induced toward real investment expenditure to tap internal net real resources (savings). If marginal productivity can be maximized from all alternative priorities, through the allocation of scarce resources combined with a competitive system, Pakistan should be able to expand the capacity of the economy in order to utilize all the available labor productivity, both in the long and short-run. This will lead to a higher level of income per capita.

Unlike the allocations of the scarce resources towards alternative priorities during the Second Five-Year Plan, the future emphasis should be for long run economic growth rather than on the short run. For the utilization of full capacity of the economy, full employment of the factors of production can and must be attained at a non-inflationary point. Lastly, the factors of production under a long-run growth model would lead to convertibility and multilateralism. Both convertibility and multilateralism ensure specialization and division of labor, thereby accentuating the self-sustained cumulative rate of net savings, especially important, for an underdeveloped economy like Pakistan.



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